88-2109

No.

In the Supreme Court of the United States

OCTOBER TERM, 1988

THE STATES OF KANSAS AND MISSOURI,
AS *PARENS PATRIAE*,
Petitioners,

vs.

THE KANSAS POWER & LIGHT COMPANY
and
UTILICORP UNITED, INC.,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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QUESTIONS PRESENTED

1. Do residential indirect purchasers of natural gas, represented *parens patriae* by their state attorneys general, have standing to sue under Section 4 of the Clayton Act, where there is an easily-proven, 100% pass-on of illegal overcharges, effected by federal and state regulations rather than by a fixed-quantity cost-plus contract?

2. Where federal and state regulations require that the full amount of any illegal overcharge be passed on by the direct purchaser in readily-identifiable form, is there an exception to the general rule barring indirect purchaser antitrust suits under Section 4 of the Clayton Act?

PARTIES

Petitioners, the States of Missouri and Kansas, acting as *parens patriae* on behalf of their residential gas consumers, are two of the six plaintiffs in a consolidated proceeding known as *In re Wyoming Tight Sands Antitrust Cases*. The States were appellants in the Tenth Circuit proceeding from which this petition arises.

Appellees in the Tenth Circuit included plaintiff The Kansas Power & Light Company ("KPL"), intervenor UtiliCorp United, Inc. ("UtiliCorp," which includes its two subsidiaries, Missouri Public Service Company and Kansas Public Service Company), and plaintiff Kansas Gas & Electric Company ("KG&E"). Plaintiff Farmland Industries, Inc. did not take part in the Tenth Circuit appeal. Because the issues raised in this Petition do not affect KG&E[1] or Farmland, only KPL and UtiliCorp are named as respondents herein.

Defendants below were Amoco Production Company ("Amoco"), Cities Service Oil & Gas Corporation ("Cities Service"), CSG Exploration Company ("CSGE"), Williams Natural Gas Company ("Pipeline") and two limited partnerships, Moxa Limited Partnership and Wamsutter Limited Partnership. Amoco, Cities Service and CSGE intervened at the Tenth Circuit, but did not take a position as to which group of plaintiffs should prevail. The other defendants did not appear in the Tenth Circuit. None of the defendants is named as a respondent herein.

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1. Plaintiff Kansas Gas & Electric is solely an electric utility that does not resell gas. The States did not oppose KG&E's motion for partial summary judgment, and have recognized throughout these proceedings that summary judgment was properly granted in favor of KG&E.

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

The States of Missouri and Kansas, appearing here in their *parens patriae* capacity on behalf of all natural persons in these States who are residential natural gas consumers, respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Tenth Circuit entered in this proceeding on January 31, 1989, in order to resolve the conflict between the Tenth and Seventh Circuit Courts of Appeals on the important issues presented herein.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Tenth Circuit that gives rise to this petition is reported at *In re Wyoming Tight Sands Antitrust Cases,* 866 F.2d 1286 (10th Cir. 1989), and is reprinted in Appendix A hereto ("App. A") at page A1. By order filed March 27, 1989, the Tenth Circuit denied the petition for rehearing and suggestions for rehearing en banc. App. B, A18.

The opinion of the United States District Court for the District of Kansas dismissing petitioners' *parens patriae* complaints is reported at *In re Wyoming Tight Sands Antitrust Cases,* 695 F. Supp. 1109 (D. Kan. 1988), App. C, A22; the district court's opinion on the motion for certification is reported at 695 F. Supp. at 1119, App. D, A40.

JURISDICTION

On May 4, 1988, the district court granted partial summary judgment in favor of the respondent utilities and dismissed the federal antitrust claims of the States of Kansas and Missouri as *parens patriae* "for lack of standing." On motion of the States, the district court on June 7, 1988, certified to the Tenth Circuit a question of *parens patriae* standing, pursuant to 28 U.S.C. § 1292(b). The Tenth Circuit accepted the Section 1292(b) appeal.

On January 31, 1989, the Tenth Circuit entered an opinion affirming the decision of the district court. A timely-filed petition for rehearing and suggestion for rehearing en banc was denied on March 27, 1989. Pursuant to 28 U.S.C. § 2101(c), this petition for certiorari has been filed within 90 days of the denial of rehearing.

The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTE INVOLVED IN THE CASE

Section 4 of the Clayton Act, 15 U.S.C. § 15(a) (1982), provides in pertinent part:

> [A]ny person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee.

STATEMENT OF THE CASE

A. Background

In 1984, 1985 and 1986, the Attorneys General for the petitioners States of Kansas and Missouri (hereinafter "the States") and three utilities filed these actions charging defendant Williams Natural Gas Company ("Pipeline") and others with selling natural gas at artificially inflated prices. The inflated prices, plaintiffs allege, were the result of a price-fixing conspiracy and other anticompetitive behavior involving Pipeline, its then-parent Cities Service Company, CSG Exploration, Amoco and two limited partnerships. The general background of the conspiracy is described in *Midwest Gas Users Association v. FERC*, 833 F.2d 341 (D.C. Cir. 1987).

The price-fixed gas was produced in Wyoming, then transported by Pipeline and sold to KPL, UtiliCorp and

other utilities in Missouri and Kansas.[2] The utilities resold the gas to various consumers, including individual residents of the two States. These gas sales occurred under a regulatory system that required *all* gas costs to be passed on by the Pipeline, through the utilities, to the end-use consumers.[3] This regulatory pass-through mechanism is mandatory; at no level of distribution is there any discretion to absorb or modify any increase in the cost of gas.[4] The effect of this pass-through on the

2. KPL and UtiliCorp are two of more than 50 gas utilities operating as regulated monopolies within defined service areas in Kansas and Missouri. Other non-party utilities provide natural gas purchased from the conspirators to over 50,000 Kansas residential consumers. The claims of these residential users will be lost if the Attorneys General cannot represent them in their *parens patriae* capacity.

3. This regulatory mechanism operates first at the federal level, where the Pipeline is regulated by the Federal Energy Regulatory Commission (FERC), pursuant to the Natural Gas Act, 15 U.S.C. §§ 717 *et seq.* (1982) (NGA), and the Natural Gas Policy Act, 15 U.S.C. §§ 3301 *et seq.* (1982) (NGPA). Under the NGA, Pipeline must adjust its rates semi-annually to reflect any changes in the price of gas paid to producers by Pipeline, in accordance with Purchased Gas Adjustment (PGA) clauses in Pipeline's tariff. 15 U.S.C. § 717(d), (e); *see* 18 C.F.R. §§ 154.1 *et seq.* (1988).

At the state level, utilities such as KPL and UtiliCorp are regulated by the Missouri Public Service Commission and the Kansas Corporation Commission. *See* Mo. Rev. Stat. §§ 386.250 (5), 393.140(1), 393.270(2) (1986); Kan. Stat. Ann. §§ 66-1,201, 66-1,206 (1985). Both state commissions enforce PGA clauses in the utilities' tariffs. UtiliCorp's KPS subsidiary operates under a PGA clause in a locally-enforced ordinance. These PGAs require that KPL and UtiliCorp automatically pass on to their customers the utilities' entire wholesale cost of gas from the Pipeline.

4. As David S. Black, President and CEO of KPL, testified before the Kansas Legislature:

> Essentially, we [KPL] provide a transportation service, and have title to the gas for the few hours required to move it from the wellhead to the burner-tip. As the cost of this gas changes, it is reflected in the customers' bills, through the operation of the purchased gas adjustment mechanism, penny-for-penny and dollar-for-dollar.

cost of gas to consumers is easy to determine—the utilities make public filings showing the volume and price of gas sold to each customer category, including residential consumers; further, the passed-on prices are reflected as a separate identifiable entry on each residential consumer's monthly gas bill from the utilities.

The Tenth Circuit, recognizing the effect of this regulatory system, *assumed* for purposes of its decision "that there was a perfect and provable pass-on of the allegedly illegal overcharge . . ." App. A, A14.

B. Proceedings Below

The utilities, in motions for partial summary judgment, argued to the district court that they alone were the proper plaintiffs and that the States lacked standing to sue because residential consumers are indirect purchasers whose claims are barred by the rule of *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968) and *Illinois Brick Company v. Illinois*, 431 U.S. 720 (1977). Although the utilities did not deny that they passed on all of the overcharges to the residential consumers, they argued that because they had no fixed-quantity contracts with these consumers, no exception to the direct-purchaser rule applied. Petitioners countered that because state and federal regulation resulted in an easily-provable and perfect pass-through of all illegal overcharges, they had standing to sue under the *Illinois Brick* exception. The district court granted summary judgment in favor of the utilities, holding that even proof of a perfect pass-on would not give the States standing, because there were no "fixed-quantity contracts." App. C, A33-34.

On interlocutory appeal, the Tenth Circuit affirmed the district court's dismissal of the States' *parens patriae*

claims. While recognizing that "there might be" an exception to the *Hanover Shoe* and *Illinois Brick* rule that only direct purchasers have standing to sue, the Tenth Circuit found no exception applicable here. Even though it assumed a perfect pass-through of damages to the consumer, the court narrowly interpreted *Illinois Brick* as *requiring* a pre-existing, fixed-quantity, cost-plus contract. The Court of Appeals held that because no "fixed-quantity contract" was present in this case, the consumers had no standing.[5]

In so holding, the Tenth Circuit squarely rejected the carefully-reasoned decision of the en banc Seventh Circuit on virtually identical facts in *State of Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Corporation*, 852 F.2d 891 (7th Cir.) (en banc), *cert. denied*, 109 S. Ct. 543 (1988).[6] There, Judge Richard Posner expressly allowed residential consumers of natural gas to maintain *parens patriae* actions. The Seventh Circuit concluded that the regulatory system under which natural gas is produced, distributed and consumed operates to alleviate any concerns expressed in *Illinois Brick*. Specifically, the Seventh Circuit found that this regulation resulted in a perfect and easily-provable pass-through of antitrust damages to residential consumers which would (1) obviate any need to apportion these damages and (2) provide state attorneys general with incentive to sue.

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5. In the Tenth Circuit's words: "To say that the utilities have a cost-plus fixed fee contract for a fixed quantity with their residential consumers would amount to fitting a square peg into a round hole. There exists no contract between the utilities and their residential consumers for any particular quantity." App. A, A12.

6. For the convenience of the Court, a copy of this decision is included in Appendix E hereto, at A43.

In rejecting the Seventh Circuit's approach, the Tenth Circuit mechanically applied certain language from *Illinois Brick* without analyzing the underlying concerns expressed by this Court. App. A, A8-13. The Tenth Circuit assumed "that there was a perfect and provable pass-on of the allegedly illegal overcharge . . . ." App. A, A14. Nevertheless, the court found that this was not a sufficient reason to allow indirect purchasers to sue for an antitrust violation:

> A perfect pass-on, standing alone, is not sufficient reason to allow an indirect purchaser to sue [sic] an alleged antitrust violation. We narrowly construe the cost-plus exception as to do otherwise would be to do that which the Supreme Court has cautioned against. We hold that the controlling cases are *Hanover Shoe* and *Illinois Brick*, and not *Panhandle Eastern*. App. A, A14-15.

The Tenth Circuit concluded that even *considering* proof of a perfect pass-on would "'entail the very problems that the *Hanover Shoe* rule was meant to avoid.' *Id.* at [431 U.S.] 744-45. We therefore hold that the amount of illegal overcharges actually passed on by the utilities to its customers is not an issue of material fact necessary to a resolution of the narrow issue before this court." App. A, A17.

The States' petition for panel rehearing and/or rehearing en banc was denied.

Thus the issue presented is purely a question of law on undisputed facts: where there exists a mandatory, readily-proven pass-through of overcharges, which holding is correct—that of the court below in this case, or that of the Seventh Circuit in *Panhandle Eastern*?

REASONS FOR GRANTING THE WRIT

The Tenth Circuit's decision in this case directly conflicts with the holding of the Seventh Circuit in *State of Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Corporation*, 852 F.2d 891 (7th Cir.) (en banc) (Posner, J.), *cert. denied*, 109 S. Ct. 543 (1988), App. E, A43. There, the en banc Seventh Circuit fleshed out the "cost-plus" exception and applied it to permit the Illinois attorney general, acting as *parens patriae* on behalf of residential gas consumers, to sue for antitrust damages. Specifically, the critical question on which the Seventh and Tenth Circuits disagree is: Do indirect purchasers, who by regulatory mandate pay *all* of the illegal antitrust overcharges, fall within an exception to the general rule that only direct purchasers of a product have standing to seek antitrust damages from antitrust violators? The Seventh Circuit says "yes"; the Tenth Circuit says "no".

This conflict has resulted because lower courts are having significant problems understanding and interpreting prior opinions of this Court. These conflicting decisions complicate the uniform administration of Section 4 of the Clayton Act and undermine the ability of state attorneys general to enforce the antitrust laws. The Court should grant certiorari and end this confusion.

More specifically, the reasons for granting certiorari may be stated as follows:

I.

The Tenth Circuit's Decision Directly Conflicts With the Seventh Circuit's En Banc Ruling in *Panhandle Eastern*.

The conflict between the decision below and the Seventh Circuit's decision in *Panhandle Eastern*, App. E, A43, is clear and complete. As the Tenth Circuit put it: "The States urge us to apply the law as enunciated in *Panhandle Eastern*, 852 F.2d 891. This we decline to do." App. A, A13.[7]

The Seventh Circuit in *Panhandle Eastern* found a complete and provable pass-through of allegedly illegal overcharges to residential consumers in Illinois. Based on this finding, the Seventh Circuit concluded that those consumers had standing to sue. The Tenth Circuit in the instant case *assumed* a 100% perfect pass-through of overcharges, yet nonetheless ruled that residential consumers were without standing, simply because they were indirect purchasers without a fixed-quantity contract.

These two cases are identical in every important factual respect. In both, state attorneys general sued to redress antitrust violations that resulted in injury to residential gas consumers. In both, the interplay between state and federal regulation required a perfect pass-on of the overcharges. In both, some or all of the utilities were also plaintiffs, despite the likelihood that any overcharges they collected might be ordered refunded to the consumers. In neither case were there problems with duplicative recovery or apportionment of shared damages, nor were there any real concerns for antitrust enforcement.

Under these circumstances, the Seventh Circuit held that the State could sue, reasoning that where the rationale for *Illinois Brick* does not apply, neither should

7. The district court also recognized the factual similarity between this case and *Panhandle Eastern*. It specifically relied on the Seventh Circuit's *panel* opinion in *Panhandle Eastern* (later reversed en banc) to support its entry of summary judgment: "Just recently the Seventh Circuit came to the same conclusion *on almost identical facts*" (emphasis added). App. B at A36.

the rule. The Tenth Circuit expressly disagreed. App. A, A13-15. The conflict is clear. Certiorari is thus appropriate.[8]

II.

The Decision Below Raises Important Issues as to the Standing of Consumers to Recover Antitrust Damages for Overcharges That Have Been Passed on to Them.

Three times this Court has suggested to lower courts that there is an exception to the general rule that only a direct purchaser has standing to recover antitrust damages: *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481, 494 (1968) ("there might be" an exception to the rule, "for instance, where an overcharged buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged"); *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 735-36 (1977) ("*Hanover Shoe* indicated the narrow scope it intended for any exception . . . by citing, as the only example . . . a pre-existing cost-plus contract"); *California v. ARC America Corp.*, 109 S. Ct. 1661, 1666 n.6 (1989) (in *Illinois Brick* "we implicitly recognized . . . that indirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them"). But the precise nature and scope

8. The *Panhandle Eastern* petition for certiorari presented two questions: (1) whether the Seventh Circuit's holding "in effect" overruled *Illinois Brick;* (2) whether "residential indirect purchasers of natural gas, who do not purchase gas pursuant to pre-existing, fixed quantity, cost-plus contracts with the direct purchaser," are barred from seeking antitrust damages by *Illinois Brick*. Those two questions mirror the ruling of the Tenth Circuit in the instant case, thus further underlining the conflict between the two Circuits.

of this exception has not been addressed or explained by this Court. The result is confusion and conflict in the lower courts.[9]

As noted in *California v. ARC America*, this Court in *Illinois Brick* was concerned "not merely that direct purchasers have sufficient incentive to bring suit under the antitrust laws . . . but rather that at least *some* party have sufficient incentive to bring suit." (Emphasis added). And the Court added in *ARC America* that "indirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them," citing *Illinois Brick*. 109 S. Ct. at 1666 n.6. The facts in the present case fit precisely the situation described in the *ARC America* footnote, thereby suggesting that the Tenth Circuit's concerns are not shared by this Court. As indirect purchasers, the present consumers have "sufficient incentive" because they are represented by vigilant state attorneys general, well aware of their *parens patriae* responsibilities.

9. This is reflected in the decisions of several district courts applying the "cost-plus" exception in a regulatory environment. In *In re New Mexico Natural Gas Antitrust Litig.*, 1982-1 Trade Cas. (CCH) ¶ 64,685 (D.N.M. 1982), the court held, on facts similar to those here, that indirect purchasers could sue because public utility regulation had created "a straight cost pass through." *Id.* at 73,722. Other district courts have rejected an exception for cost-plus rate regulation. *See Go-Tane Service Stations, Inc. v. Ashland Oil, Inc.*, 508 F. Supp. 200 (N.D. Ill. 1981); *City of Cleveland v. Cleveland Elec. Illuminating Co.*, 538 F. Supp. 1306, 1323-24 (N.D. Ohio 1980); *U.S. Oil Co. v. Koch Refining Co.*, 518 F. Supp. 957, 962-63 (E.D. Wis. 1981). *See also In re Beef Indus. Antitrust Litig.*, 600 F.2d 1148 (5th Cir. 1979), *cert. denied*, 449 U.S. 905 (1980) (applying a test using the "functional equivalent" of a cost-plus contract).

And precisely because the gas utilities are highly regulated by the states and the overcharges are easily retrieved from public filings, this is also a case "in which it would be easy to prove the extent to which the overcharge was passed on to them [the residential gas consumers]."

If the Court is ever to explicitly recognize an exception to the direct-purchaser rule, this case presents the ideal opportunity. Each of this Court's underlying concerns in *Illinois Brick* is satisfied on the present record. Not only is the pass-on of overcharges complete and automatic, but it is easily shown by uncomplicated proof. Not only are the ultimate consumers the truly-injured parties, but here they have ample incentive to sue through their state attorneys general as *parens patriae*.

The Tenth Circuit ignored the underlying rationale of *Illinois Brick* and *Hanover Shoe*, choosing instead to rigidly apply the "fixed-quantity cost-plus contract" language of *Illinois Brick*. Is the Tenth Circuit correct? Must a pass-on arrangement always be accompanied by a cost-plus contractual obligation to purchase a fixed amount of the product? Or, as Judge Posner recognized, is it enough that the direct purchaser "acts like" a fixed-quantity reseller, with every incentive to pass on the entire overcharge? *See Panhandle Eastern*, App. E, A52-53. Would recognition of the standing of residential consumers to seek antitrust damages, in the context of a highly regulated industry, truly require—in the words of the Tenth Circuit—"carving out yet another exception (regulation of public utilities) to the basic rule that only a direct purchaser may sue for the antitrust violation"? App. A, A15.

This Court should grant certiorari to determine if residential gas consumers who are forced to absorb all the illegal overcharges, and who have sufficient incentive when represented by their state attorney general, have standing to seek treble antitrust damages. Does this situation constitute an exception to the basic rule that only direct purchasers have standing? Is this not precisely the situation contemplated in the *ARC America* footnote? None of these questions are answered by *Hanover Shoe*, *Illinois Brick*, or *ARC America*. But they are questions that repeatedly plague the lower courts, as shown by the conflict here. The Tenth Circuit decision squarely presents these questions. They are questions that deserve answers by this Court.

III.

The Issues in This Case Are Important to the Attorneys General of All Fifty States.

The Tenth Circuit's decision, barring the Attorneys General of Missouri and Kansas from suing to protect their residential gas consumers from antitrust violations, creates profound problems for attorneys general in all the States. The Kansas Attorney General, residing in the Tenth Circuit, cannot bring suit for his State's citizens. Nor can the attorneys general of other states, if suit is filed in the Tenth Circuit. But in the Seventh Circuit, these same suits by attorneys general may proceed without hindrance. Which decision should guide the actions of attorneys general in the other Circuits? The Sherman Act contemplates uniform interpretation and application across the United States. The conflict posed by the Seventh and Tenth Circuit decisions renders such uniformity impossible.

Congress placed state attorneys general in a preferred position in the enforcement of federal antitrust laws. The Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 15c (1982), "carves out a special place for state governments in enforcing federal antitrust laws." *In re Grand Jury Investigation of Cuisinarts, Inc.*, 665 F.2d 24, 35 (2d Cir. 1981). "In effect, the thrust of Title III of the Act was to overcome obstacles to private class actions through enabling state attorneys general to function more efficiently as consumer advocates." *Id.; see also* H.R. Rep. No. 499, 94th Cong., 2d Sess. 8 *reprinted in* 1976 U.S. Code Cong. & Admin. News 2578. The purpose of the Act—efficient enforcement of antitrust laws by the states—has been frustrated by the Tenth Circuit's substitution of private utilities as antitrust plaintiffs in lieu of state attorneys general.

The attorneys general have been left in a quandary as to the limits of their *parens patriae* authority in antitrust actions. While the Hart-Scott-Rodino Act and the *Panhandle Eastern* decision grant broad authority to state attorneys general, the decision below severely limits that authority and restricts the right of consumers to recover for injuries they have suffered. Thus both consumers and state attorneys general are vitally concerned that the Tenth Circuit's ruling be reviewed by this Court.

CONCLUSION

For the foregoing reasons, this petition for writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX

APPENDIX A

(Filed January 31, 1989)

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

Nos. 88-2158
88-2159

In re

WYOMING TIGHT SANDS ANTITRUST CASES.

STATE OF KANSAS, as parens patriae on behalf of natural person residing in Kansas, ROBERT T. STEPHAN, Attorney General of the State of Kansas,

and

STATE OF MISSOURI,
Plaintiffs-Appellants,

KANSAS POWER & LIGHT COMPANY, a Kansas Corporation; KANSAS GAS & ELECTRIC COMPANY,
Plaintiffs-Appellees,

UTILICORP UNITED INC.,
Plaintiff-interventor-Appellee.

v.

AMOCO PRODUCTION CO.; CITIES SERVICE OIL AND GAS CORPORATION, f/k/a Cities Service Company; CSG EXPLORATION COM-

PANY; WILLIAMS NATURAL GAS COMPANY, f/k/a Northwest Central Pipeline Corporation; THE WAMSUTTER LIMITED PARTNERSHIP; THE MOXA LIMITED PARTNERSHIP,
Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF KANSAS
(D.C. Lead No. CIV. 85-2349-S)

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Before SEYMOUR, MOORE, and BRORBY, Circuit Judges.

BRORBY, Circuit Judge.

This appeal involves a single issue: May residential consumers who are indirect purchasers of natural gas maintain an antitrust suit against the alleged antitrust violators?

I.

Three investor-owned public utilities, the Kansas Power & Light Company, Kansas Gas & Electric Company, and UtiliCorp United Inc., filed separate complaints against defendants Amoco Production Co., Cities Service Oil and Gas Corporation, CSG Exploration Company, The Moxa Limited Partnership, and The Wamsutter Limited Partnership, alleging, *inter alia*, that all defendants illegally conspired to artificially inflate the price of natural gas produced from various natural gas fields in Wyoming. The gas was then transported and sold to the public util-

ities by the conspiring defendant, Williams Natural Gas Company, an interstate pipeline company.

The states of Kansas and Missouri (the States) filed similar suits wherein basically they asserted two types of claims against the same defendants: (1) on behalf of residential consumers who purchased natural gas from the public utilities, the States acting in a *parens patriae* capacity; and (2) on behalf of state agencies, municipalities, and other political subdivisions that purchased gas directly from Williams Natural Gas Company. These suits were consolidated.

The defendants asserted various defenses, including allegations that the public utility plaintiffs lack standing under § 4 of the Clayton Act, 15 U.S.C. § 15 (1982), in that plaintiffs had not been injured in their business or property because the public utilities had passed on illegal increases in the price of natural gas to the ultimate consumer who paid the entire cost of antitrust injuries. The public utilities then filed motions for summary judgment to prohibit these pass-on defenses under *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968).

The trial court granted partial summary judgment in favor of the public utilities prohibiting the use by the defendants of the pass-on defense. The trial court characterized the motions as "in reality, motions to dismiss the States of Kansas and Missouri in their *parens patriae* capacity," and *sua sponte* dismissed the *parens patriae* claims asserted by the States.

The trial court's thorough and analytical Memorandum and Order may be found in *In re Wyoming Tight Sands Antitrust Cases*, 695 F. Supp. 1109 (D. Kan. 1988).

The States sought and obtained interlocutory appellate review of a certified question. The public utilities are the appellees. The defendants are not involved in this appeal. At the request of the States, the question certified to the court pursuant to 28 U.S.C. § 1292(b) is as follows:

> In a private antitrust action under 15 U.S.C. § 15 involving claims of price fixing against the producers of natural gas, is a State a proper plaintiff as *parens patriae* for its citizens who paid inflated prices for natural gas, when the lawsuit already includes as plaintiffs those public utilities who paid the inflated prices upon direct purchase from the producers and who subsequently passed on most or all of the price increase to the citizens of the State?

Wyoming Tight Sands, 695 F. Supp. at 1120.

The States now quarrel with the certified question. The States point out that all of the utilities that purchased the alleged price-fixed gas are not present as plaintiffs and assert that *all* of the illegal overcharges were passed on to residential consumers. The utilities assert the proposed modifications to the question are irrelevant to the issues in this appeal, and ask us to disregard the proposed factual allegations and consider the question certified by the district court.

This court will answer the question certified to us by the district court for the reasons contained in the body of this opinion.

II.

The defendant Williams Natural Gas Company is alleged to have transported natural gas from gas fields in Wyoming and sold it to the public utilities. The remain-

ing defendants, being the producers of the natural gas, are alleged to have conspired with Williams Natural Gas Company, the pipeline company, to artificially inflate the price of the natural gas.

The public utilities have sold or used the natural gas purchased from the pipeline company in different ways and therefore occupy different levels in the distribution chain. Kansas Gas & Electric Company purchased gas directly from the pipeline company for use in generating electricity, and the electricity was then sold and delivered to commercial, industrial and residential customers. Kansas Power & Light Company and UtiliCorp United Inc. purchased natural gas directly from the pipeline company for their own industrial use and for delivery to commercial, industrial and residential consumers. All three of the public utilities operate as regulated monopolies within defined service areas.

The trial court made no findings of fact concerning how much of the natural gas overcharges were passed on to the commercial, industrial and residential consumers. The States offered evidence that all the overcharges were passed on to the ultimate consumers. The trial court apparently based its partial summary judgment upon the theory that there was no need to decide whether the allegedly illegal overcharges were passed on in whole or part. The question certified to us states that "most or all" of the price increase was passed on to the consumers.

The states of Kansas and Missouri are bringing two claims. The first relates to direct purchases of natural gas made by the States and its various instrumentalities. This claim is not now before this court. The States' second claim is in its capacity as *parens patriae* on behalf of natural persons residing therein who are residential in-

direct purchasers of natural gas.[1] This is the claim we now decide.

III.

The States acknowledge the basic rule as set forth in *Hanover Shoe*, 392 U.S. 481, and as expanded in *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977). These cases hold that only the direct purchaser, and no other in the distribution chain, is the "party injured" within the meaning of § 4 of the Clayton Antitrust Act, 15 U.S.C. § 15. Stated differently, only the direct purchaser may sue for and recover the full amount of the illegal overcharge.

All rules have exceptions, and the basic rule set forth above has at least two, the cost-plus exception and the control exception. The States contend they fall squarely into either or both of these exceptions and should therefore be allowed to proceed with their suits on behalf of the residential consumers. The States, in their joint reply brief, concede the utilities' right to sue for and recover the alleged damages on behalf of the commercial and industrial customers of the utilities.

The first exception to the basic rule is what we have labeled as the cost-plus exception. The genesis of this exception may be found in *Hanover Shoe*. There the Supreme Court recognized that "there might be" an exception to the rule "for instance, when an overcharged

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1. It should be noted that §§ 4C through 4H of the Clayton Act, 15 U.S.C. §§ 15c through 15h, which is sometimes described as the Hart-Scott-Rodino Antitrust Improvements Act of 1976, empowers state attorneys general to bring treble-damage actions as *parens patriae* on behalf of resident natural persons "for injury sustained . . . to their property" by reason of any Sherman Act violations. The parties have not argued that this law eliminates the basic rule that only a direct purchaser may sue. We assume that this statutory provision comes into play when the individual consumers are the direct purchasers.

buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged." *Id.* at 494. The Supreme Court further elaborated on this exception in *Illinois Brick* when it said:

> *Hanover Shoe* indicated the narrow scope it intended for any exception . . . by citing, as the only example . . . a pre-existing cost-plus contract. In such a situation, the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price.

Id. at 735-36. We interpret this exception as requiring a pre-existing cost-plus contract for a fixed quantity. We also note the Supreme Court did not say this would constitute an exception but rather that it "might be," and for this reason we have narrowly construed the exception as also requiring a fixed quantity.

The States now assert that their system of price regulation of natural gas utilities creates a cost-plus pricing arrangement that, coupled with the residential consumers' need to purchase their full requirements of natural gas from the utilities, places the residential consumers squarely within the cost-plus exception. In making this assertion, the States place great reliance on *State ex. rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (7th Cir.), *cert. denied*, 109 S.Ct. 543 (1988).

Prior to analyzing the States' contentions, we must delve deeper into *Hanover Shoe* and then into *Illinois Brick*, as we can glean several principles therefrom to guide us in deciding this case. The direct purchaser is entitled to damages if he raises the price for his own product. *Hanover Shoe*, 392 U.S. at 489. Considerations of *stare decisis* weigh heavily in the area of statutory con-

struction where Congress is free to change the Supreme Court's interpretation of its language. *Illinois Brick*, 431 U.S. at 736. New dimensions of complexity would be added to treble-damage suits and seriously undermine their effectiveness if massive efforts were made to apportion the recovery among all potential plaintiffs. *Id.* at 737. There exists a serious problem of measuring the change in quantities of the natural gas purchased by consumers in response to a change in price. *Id.* at 742. There should be no exceptions to the basic rule for particular types of markets. *Id.* at 744. The increase in complexity of treble-damage suits will result in a reduction in the effectiveness of these suits. *Id.* at 745. There is a long-standing policy of encouraging vigorous private enforcement of the antitrust laws. *Id.* at 745.

We may distill these principles and summarize them by stating that the reasons given by the Supreme Court to justify its interpretation of the statute in *Hanover Shoe* and *Illinois Brick* are: (1) *stare decisis;* (2) encourage vigorous enforcement of the antitrust laws by reducing the expense of trial by eliminating unnecessary complications; (3) give to the direct purchaser an incentive to discover and prosecute antitrust violations; (4) avoid the problems of apportionment of damages; and (5) exceptions to the basic rule are to be narrow in scope.

First, as to *stare decisis*. *Illinois Brick* contains a message to Congress as well as to students of the law. That message is simple. The phrase "[a]ny person who shall be injured" as used in § 4 of the Clayton Act means only a direct purchaser from the antitrust violator. In short, *stare decisis* requires that when a decision of the Supreme Court is made, it is binding on courts of appeals. In this case, the rule is clear, and the Supreme Court has

cautioned us concerning expansions to the exception. Were we to broadly construe the exceptions, we would also be diluting the clear message given to Congress concerning the Supreme Court's construction of § 4 of the Clayton Act.

Second, as to avoiding adding complexity and expense to antitrust suits. Were we to construe the law to allow the States to pursue their *parens patriae* claims, then unnecessary issues would be added to the trial, including the unresolved factual issue of how much of the alleged illegal overcharge was passed on to the residential consumers of each utility. If all overcharges were passed on, then allowing the consumers to prove and collect the damages could result in the antitrust violators escaping the payment of damages relating to decreased demand by residential consumers due to the higher price. Complex issues of proof will grow geometrically if the States press their consumers' demands, unless we should rule as a matter of law that the utilities' share of the alleged damages are likewise passed on to the consumers. This we are not prepared to do, given the factual record before us. The question certified to us provides that "most or all" of the illegal price increase was passed on.

Third, as to giving the direct purchaser an incentive to discover and prosecute the antitrust violator. It can be argued that enforcement of the antitrust laws would not be imperiled by allowing the States to pursue their claims in this case. But what of the next case? By removing an incentive for a utility to discover and enforce antitrust violations, would we not be shifting the incentive to an indirect purchaser? Would we not be shifting the cost of policing and enforcing the antitrust laws to the states? Would we not be undercutting the basic rationale

for the Supreme Court's decisions in *Hanover Shoe* and *Illinois Brick?* As stated by the Supreme Court in *Hanover Shoe*:

> [A]ntitrust laws will be more effectively enforced by concentrating the full recovery for the overcharge in the direct purchasers rather than by allowing every plaintiff potentially affected by the overcharge to sue only for the amount it could show was absorbed by it.

Id. at 735.

The argument can be made that the utility really has no incentive to sue because the public utility regulatory commission of the state may force the utility to pass on to the consumers all damages the utility may recover. This is a question we do not answer. If is sufficient to state that a utility filed first in this case. It should also be noted that the utilities' motions to strike the pass-on defense asserted by the gas suppliers and transporters was characterized by the trial court as being in reality a motion to strike the States' *parens patriae* claim. It is reasonable to assume that the public utilities must believe there is something for their benefit in pursuing these actions. Allowing the States to press the claims of the indirect purchasers will result in the probability that direct purchasers will fail to discover and aggressively assert antitrust claims.

Fourth, as to apportioning damages. The States assert there is no problem in apportioning the hoped-for damages in this case. They contend that it is a simple matter of proving how much natural gas went to the residential consumers and multiplying this by the unit illegal overcharge. The States may have an overly simplistic view of this problem and may not have considered

the nature of the defenses which will probably be asserted at trial. Any allocation of illegal overcharges to the residential consumers may require tracing the sale from the wellhead through each level of distribution in order to establish the amount of illegal gas costs actually paid by the consumers in each state, probably resulting in exactly that which the Supreme Court prohibited, i.e., adding new dimensions of complexity to antitrust suits. There is no way this court could or would instruct the parties on proof of damages prior to trial as there are too many facts not now known. Suffice it to say that apportioning damages will probably not be as simple as contended by the States.

Looking at the rationales underlying the basic rule, we are of the opinion that to allow the cost-plus exception urged upon us by the States would undercut the very reasons for the basic rule.

Fifth, as to the words of the exception itself. To say that the utilities have a cost-plus fixed fee contract for a fixed quantity with their residential consumers would amount to fitting a square peg into a round hole. There exists no contract between the utilities and their residential consumers for any particular quantity. Obviously a residential consumer could stop using natural gas and convert to an alternative source of energy such as wood or coal, or a consumer could decrease the quantity of natural gas used. The apparent reason for the fixed-quantity requirement to the cost-plus exception is simply that there would exist no problem of apportionment between the direct and indirect purchasers. In this case, the problem of apportionment would exist even if all of the overcharge was passed on, because there still exists the issue of decreased residential demand caused by the

higher price. We hold that suit by residential consumers of natural gas who are not direct purchasers does not lie within the cost-plus exception to the basic rule.

The States urge us to apply the law as enunciated in *Panhandle Eastern*, 852 F.2d 891. This we decline to do.

Panhandle Eastern held, in effect, that the purchased gas adjustment component of gas utility regulation, coupled with the fact that residential consumers are obligated to purchase their full requirements of natural gas from monopolistic utilities, placed the residential consumer squarely within the cost-plus exception of *Hanover Shoe* and *Illinois Brick*.

We distinguish the facts of this case from those in *Panhandle Eastern*. In *Panhandle Eastern*, there was formal cost-plus pricing (as we may have here); a contract that required 100 percent passing on (as we may or may not have here);[2] and an acknowledgment of 100 percent pass-on in every kilowatt-hour resold to the utilities' residential consumers (which we may or may not have here). In *Panhandle Eastern* the utility had delayed in filing suit, and there was a serious question as to whether or not the statute of limitations had expired. In *Panhandle Eastern* the court was dealing with the residential consumers of a single utility; here we are dealing with utilities that occupy different levels on the distribution chain within two states, and with two states and their attendant public utility rate regulation schemes. In this

2. In this case, there is a purchased-gas adjustment clause in the rate tariffs of Kansas Power & Light. There is an energy-cost adjustment clause, which operates in a similar manner, in Kansas Gas & Electric's operating tariff in Kansas. In Lawrence, Kansas, the Kansas Public Service Company, a division of UtiliCorp, did not resell natural gas by way of a purchased-gas adjustment clause mechanism.

case we have yet another unresolved factual issue: UtiliCorp asserts in its brief that more of the allegedly illegal overcharges could be recovered if the utilities were allowed to press the claims of the residential consumers, an assertion which the court in *Panhandle Eastern* apparently did not face. The Seventh Circuit itself stated in *Panhandle Eastern* that this case (*Wyoming Tight Sands*, 695 F. Supp. 1109) was distinguishable from *Panhandle Eastern*. 852 U.S. at 893. The most important difference between *Panhandle Eastern* and this case may be that there was apparently no doubt in *Panhandle Eastern* that the entire overcharge was passed on, and there was no need to apportion damages between the direct and indirect purchasers. In this case, the amount of the overcharge passed on may be an unresolved question of fact. However, even if we assume, as we do for the purpose of deciding the issues before us, that there was a perfect and provable pass-on of the allegedly illegal overcharge, we are not persuaded that the facts of this case would place this case into the narrow exception to the rule. At the most, a perfect pass-on might solve the problem of apportioning damages between the direct and indirect purchaser but for the issue of decreased demand due to higher prices. This does not justify shifting the incentive to prosecute alleged antitrust violations from the direct purchaser, who is the closest to the violator and who presumably has the better knowledge, to the indirect purchaser. A perfect pass-on of all illegal overcharges may exist in a model world but probably does not exist in the real world. A perfect pass-on, standing alone, is not sufficient reason to allow an indirect purchaser to sue an alleged antitrust violation. We narrowly construe the cost-plus exception as to do otherwise would be to do that which the Supreme Court has cautioned against. We

hold the controlling cases are *Hanover Shoe* and *Illinois Brick*, and not *Panhandle Eastern*.

The States also rely upon *In re New Mexico Natural Gas Antitrust Litig.*, 1982-1 Trade Cases ¶ 64,685 (D.N.M. 1982). We distinguish this case, as the direct purchasers were billing their consumers monthly and separately for a "cost of gas component," and perhaps more importantly, the residential consumers constituted the first direct purchasers from the conspiring defendants.

We are not persuaded that the cost-plus contract exception of *Hanover Shoe* is applicable to the facts of this case. If we were to adopt the reasoning of *Panhandle Eastern*, we would in reality be carving out yet another exception (regulation of public utilities) to the basic rule that only a direct purchaser may sue for the antitrust violation, and this we are unwilling to do.

IV.

In *Illinois Brick*, the Supreme Court set forth another situation where the pass-on defense "might be" permitted, and that is where the direct purchaser is owned or controlled by its customer. *Id.* at 736 n.16.

The States argue that as they exercise plenary authority over the utilities, particularly with regard to rates, this fact equates to placing the States within the control exception. We do not agree. As the trial court stated: "The utilities are for-profit, publicly held corporations and simply do not fit within this exception." *Wyoming Tight Sands*, 695 F. Supp. at 1117. Calling a cow a horse does not make it so. State regulation of utility rates does not give to the states or its citizens ownership or control of the public utilities. We hold that the public utilities

in this case are neither owned nor controlled by its customers, and we therefore conclude that the "control exception" does not apply to this controversy.

V.

The States next assert that allowing residential consumers to sue is fully consistent with the prior decisions of this court, citing *Central Nat'l Bank v. Rainbolt*, 720 F.2d 1183 (10th Cir. 1983); *Zinser v. Continental Grain Co.*, 660 F.2d 754 (10th Cir. 1981), *cert. denied*, 455 U.S. 941 (1982); and *Jones v. Ford Motor Co.*, 599 F.2d 394 (10th Cir. 1979). These cases are inapposite. None involves pass-on or cost-plus contracts.

The States next urge that *Illinois Brick* should not be read as a rigid bar to recovery on the part of all indirect purchasers and cite *Blue Shield of Virginia v. McCready*, 457 U.S. 465 (1982), wherein plaintiff was allowed to maintain an antitrust suit as she was the person who was "out of pocket" by paying her psychologist when Blue Shield was exerting coercive pressure to induce its subscribers into selecting psychiatrists over psychologists, and *Associated Gen. Contractors of California, Inc. v. California State Council of Carpenters*, 459 U.S. 519 (1983), wherein the Supreme Court held that a decision as to antitrust standing requires a case-by-case analysis of at least six factors.

These cases are distinguishable. In *Blue Shield*, the Supreme Court held that plaintiff was in essence the direct purchaser when it stated "it is not the employer as purchaser, but its employees as subscribers, who are out of pocket as a consequence of the plan's failure to pay benefits." *Id.* at 475. The Court held that McCready had paid her psychologist; Blue Shield failed to pay her; and

McCready's psychologist could link no claim of injury to himself arising from his treatment of McCready. In the instant case, the residential user of gas paid the utility and the utility can assert a claim of injury for decreased consumer demand. In *Associated Gen. Contractors*, the Supreme Court applied the policies underlying *Illinois Brick*, and dismissed the claims of a labor union for indirect damages, holding that the union's claim of consequential harm was insufficient as a matter of law. *Id.* at 545.

The States assert that the trial court should not have granted partial summary judgment as there may exist a genuine issue of material fact, i.e., did the utilities pass on all of the overcharges. In *Illinois Brick*, the Supreme Court stated, "[T]he process of classifying various market situations according to the amount of pass-on likely to be involved and its susceptibility of proof in a judicial forum would entail the very problems that the *Hanover Shoe* rule was meant to avoid." *Id.* at 744-45. We therefore hold that the amount of illegal overcharges actually passed on by the utilities to its customers is not an issue of material fact necessary to a resolution of the narrow issue before this court.

We conclude that residential indirect purchasers of natural gas are not entitled to sue the alleged violators under either *Hanover Shoe* or *Illinois Brick*. The question certified to us is answered in the negative, and the judgment of the trial court, insofar as is necessary to answer the question certified, is AFFIRMED.

APPENDIX B

(Filed March 27, 1989)

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

Nos. 88-2158
88-2159

In Re:

WYOMING TIGHT SANDS ANTITRUST CASES.

THE STATE OF KANSAS, as parens patriae on behalf of natural person residing in Kansas, ROBERT T. STEPHAN, Attorney General of the State of Kansas,

and

STATE OF MISSOURI,
Plaintiffs-Appellants,

KANSAS POWER & LIGHT COMPANY, a Kansas Corporation, KANSAS GAS & ELECTRIC COMPANY,
Plaintiffs-Appellees,

UTILICORP UNITED INC.,
Plaintiff-intervenor-Appellee,

v.

AMOCO PRODUCTION CO., CITIES SERVICE OIL AND GAS CORPORATION, f/k/a Cities Service Company, CSG EXPLORATION COMPANY, WILLIAMS NATURAL GAS COMPANY, f/k/a Northwest Central Pipeline Corporation, THE WAMSUTTER LIMITED PARTNERSHIP, THE MOXA LIMITED PARTNERSHIP,
Defendants-Appellees.

ORDER

Before Holloway, McKay, Seymour, Moore, Tacha, Baldock, and Brorby, Circuit Judges.

This matter comes on for consideration of appellants' joint petition for rehearing and suggestion for rehearing en banc.

Upon consideration whereof, the petition for rehearing is denied by the panel to whom the case was argued and submitted.

In accordance with Rule 35(b) of the Federal Rules of Appellate Procedure, the petition for rehearing and suggestion for rehearing en banc were transmitted to all the judges of the court in regular active service. No member of the hearing panel and no judge in regular active service on the court having requested that the court be polled on rehearing en banc, Rule 35, Federal Rules of Appellate Procedure, the suggestion for rehearing en banc is denied.

Judges Logan, Anderson and Ebel did not participate.

Entered for the Court

Robert L. Hoecker
Clerk
By: /s/ Patrick Fisher
Patrick Fisher
Chief Deputy Clerk

(Filed April 6, 1989)

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

JANUARY 31, 1989.

Before the Honorable Stephanie K. Seymour, Honorable John P. Moore and Honorable Wade Brorby, Circuit Judges.

Nos. 88-2158
88-2159
(D.C. Lead No. CIV 85-2349-S)

In re

WYOMING TIGHT SANDS ANTITRUST CASES.

STATE OF KANSAS, as parens patriae on behalf of natural person residing in Kansas, ROBERT T. STEPHAN, Attorney General of the State of Kansas,

and

STATE OF MISSOURI,
Plaintiffs-Appellants,

KANSAS POWER & LIGHT COMPANY, a Kansas Corporation; KANSAS GAS & ELECTRIC COMPANY,
Plaintiffs-Appellees,

UTILICORP UNITED INC.,
Plaintiff-intervenor-Appellee.

v.

AMOCO PRODUCTION CO.; CITIES SERVICE OIL AND GAS CORPORATION, f/k/a Cities Ser-

vice Company; CSG EXPLORATION COMPANY; WILLIAMS NATURAL GAS COMPANY, f/k/a Northwest Central Pipeline Corporation; THE WAMSUTTER LIMITED PARTNERSHIP; THE MOXA LIMITED PARTNERSHIP,
Defendants-Appellees.

JUDGMENT

This cause came on to be heard on the record on appeal from the United States District Court for the District of Kansas, and was argued by counsel.

Upon consideration whereof, it is ordered that the judgment of that court is affirmed.

ROBERT L. HOECKER
Clerk
By /s/ Patrick Fisher
Patrick Fisher
Chief Deputy Clerk

APPENDIX C

(Filed May 4, 1988)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF KANSAS

CIVIL ACTION NO. 85-2349-S
& CONSOLIDATED CASES

IN RE

WYOMING TIGHT SANDS
ANTITRUST CASES

MEMORANDUM AND ORDER

These consolidated actions concern allegations that certain suppliers of natural gas conspired to fix inflated prices in violation of the federal antitrust laws. Several distinct categories of plaintiffs are suing several distinct categories of defendants. The issue presently before the court is ultimately one of standing: Who are the proper parties to assert the antitrust claims?

I.

The facts can be simplified for purposes of the present dispute. Three companies (defendants Amoco Production Company, CSG Exploration Company, and Cities Service Oil and Gas Corporation) and two limited partnerships formed by the companies (defendants Moxa Limited Partnership and Wamsutter Limited Partnership) produced natural gas out of the Wyoming Tight Sands formation in the State of Wyoming. The companies, through the limited partnerships, contractually committed certain amounts

of natural gas to the successors of defendant Williams Natural Gas Company (Cities Service Gas Company (CSGC), and Northwest Energy Company (NWC)), which operated an interstate pipeline and which had an affiliation with CSG. *See generally Midwest Gas Users Ass'n v. FERC*, 833 F.2d 341, 345-49 & nn. 3-5 (D.C. Cir. 1987) (discussing the background of the various actors in this controversy). The allegation is that these six entities (the three producing companies, two producing limited partnerships, and the pipeline) conspired to inflate prices.

The plaintiffs represent several vertical levels in relation to the pipeline. Farmland Industries, Inc. is an agricultural concern that purchased gas directly from the pipeline for its own consumption. Kansas Gas and Electric (KG&E) is a public utility that purchased gas directly for use in generating electricity, which was then delivered to industrial and residential consumers. Kansas Power and Light Company (KP&L) and Utilicorp United, Inc. (Utilicorp) are public utilities that purchased gas directly from the pipeline for their own industrial use and for delivery to industrial and residential consumers. The States of Kansas and Missouri have asserted two types of claims: (1) On behalf of residential consumers who purchased gas from the utilities, the States are in this lawsuit in a *parens patriae* capacity; and (2) On behalf of state agencies, municipalities, and other political subdivisions that purchased gas directly from the pipeline, the States are suing in a representative capacity. *See* Appendix to this Memorandum and Order (charting the vertical and horizontal relationships of the parties). The damages asserted by all plaintiffs arise from the allegedly illegal inflation of the price of natural gas. All plaintiffs seek reimbursement for the overcharge (along with the treble damage award in 15 U.S.C. § 15), with the utilities also alleging

that the illegally inflated price of natural gas caused a decrease in consumer consumption and a corresponding decrease in profits. The utilities contend that because their rates are regulated, their profits are directly related to consumer demand.

Plaintiffs KG&E and KP&L and plaintiff-intervenor Utilicorp have moved to strike certain defenses or, in the alternative, for partial summary judgment. The defenses they seek to strike deal with the "pass-on" theory of avoiding antitrust liability. Section 4 of the Clayton Act grants certain persons standing to bring an antitrust lawsuit:

> [A]ny person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained . . . .

15 U.S.C. § 15 (1982). Defendants Cities Service Oil & Gas Corporation, GSG Exploration Company, Amoco Production Company, and Williams Natural Gas Company have asserted numerous defenses, including allegations that the public utility plaintiffs (1) lack standing under Section 4 and (2) have not been injured in their business or property under Section 4. These defendants allege that the utilities have passed on dollar-for-dollar any illegal increase in the price of natural gas, so that the consumer has borne the entire cost of any antitrust injury. This is the "pass-on" defense. The United States Supreme Court has abolished the pass-on theory, with several narrow exceptions. Defendants assert that these exceptions apply in this case.

II.

In *Hanover Shoe, Inc. v. United Shoe Mach. Corp.*, 392 U.S. 481 (1968), a manufacturer of shoes sued a manufacturer and distributor of shoe machinery for violations of the Sherman Act, 15 U.S.C. § 4, alleging that the latter's practice of leasing and refusing to sell its more complicated and important shoe machinery was an instrument of unlawful monopolization. 392 U.S. at 483. United Shoe Machinery, the machine manufacturer, claimed that plaintiff Hanover Shoe suffered no legally cognizable injury, because the illegal overcharge was allegedly reflected in the price of Hanover's shoes, so that the consumer suffered the actual monetary injury. The court did not dispute the premise of this argument, but it found that Hanover Shoe was nevertheless entitled to bring the damage action:

> We hold that the buyer is equally entitled to damages if he raises the price for his product. As long as the seller continues to charge the illegal price, he takes from the buyer more than the law allows. At whatever price the buyer sells, the price he pays the seller remains illegally high, and his profits would be greater were his costs lower.

Id. at 489. The Court noted with approval a line of cases in which the possibility that a plaintiff had recouped the overcharges from its customers was found to be irrelevant in assessing damages. *Id.* at 490. As an example of such a situation, the Court discussed a case in which it was alleged that a shipper of goods should not recover in an antitrust lawsuit against a common carrier railroad because the shipper is able to simply pass on to its customers an illegally high charge:

> "The general tendency of the law, in regard to damages at least, is not to go beyond the first step. As it does not attribute remote consequences to a defendant so it holds him liable if proximately the plaintiff has suffered a loss. The plaintiffs suffered losses to the amount of the verdict when they paid. Their claim accrued at once in the theory of the law and it does not inquire into later events. . . . The carrier [*i.e.*, the railroad] ought not to be allowed to retain his illegal profit, and the only one who can take it from him is the one that alone was in relation with him, and from who the carrier took the sum. . . . Probably in the end the public pays the damages in most cases of compensated torts."

Id. at 490-91 n.8 (quoting *Southern Pac. Co. v. Darnell-Taenzer Lumber Co.*, 245 U.S. 531, 533-34 (1918)). *See also Associated General Contractors of Cal., Inc. v. California State Council of Carpenters*, 459 U.S. 519, 534 & n.30 (1983). This analysis is particularly appropriate in the present case, because the utilities have been analogized as being mere shippers or transporters of natural gas from the wellhead to the consumer.

The *Hanover Shoe* Court did recognize at least one possible exception to the unavailability of the pass-on defense—"when an overcharged buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged." 392 U.S. at 494. In so stating, the Supreme Court appeared to be referring to a discussion earlier in the opinion, in which the court justified elimination of the pass-on defense based on the "insurmountable" task of making a convincing showing on each element necessary to establish the applicability of the defense. The elements of the defense were: (1) The buyer

raised his price in response to, and in the amount of, the overcharge; (2) The buyer's margin of profit and total sales had not thereafter declined; and (3) The buyer could not or would not have raised his prices absent the overcharge or maintained the higher price had the overcharge been discontinued. 392 U.S. at 493. The only foreseeable instance in which these elements could be established would have been a fixed quantity, cost-plus contract, thereby creating the exception.

The other major Supreme Court opinion involving the pass-on defense was *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977). The ultimate holding of the *Illinois Brick* Court was that the *Hanover Shoe* analysis, which established the unavailability of the pass-on defense to a monopolizing manufacturer in a case brought by a direct purchaser-middleman, applies equally to an indirect purchaser-consumer who attempts to use the pass-on theory offensively by asserting that he has suffered the antitrust injury because the direct purchaser has passed on the entire illegal price increase. While the holding is certainly relevant to the present facts, of equal importance is the Court's interpretation and application of *Hanover Shoe*, along with an explanation of the scope of the exceptions to the general rule.

The defendants in *Illinois Brick* were manufacturers and distributors of concrete block. Their principal buyers were masonry contractors, who submitted bids to general contractors for the masonry portions of construction projects. In turn, the general contractors submitted bids for the overall construction project to customers such as the State of Illinois and its political subdivisions. The State of Illinois, on behalf of in itself and its political subdivisions, filed an antitrust action against the defendants,

alleging that the latter had engaged in a combination and conspiracy to fix prices in violation of section 1 of the Sherman Act, 15 U.S.C. § 1. If all or part of the illegal overcharge was passed on by the masonry and general contractors to the plaintiffs, then seemingly the plaintiffs had been "injured in [their] person or property" under section 4 of the Clayton Act. 431 U.S. at 726-27.

The *Illinois Brick* Court reemphasized both the basic principle that the pass-on theory is not available in antitrust litigation and the limited role that any exception could be allowed to play. The Court acknowledged two possible exceptions. The first was the *Hanover Shoe* cost-plus exception:

> In such a situation, the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price. The effect of the overcharge is essentially determined in advance, without reference to the interaction of supply and demand that complicates the determination in the general case.

431 U.S. at 736.* As for the second, the Court noted in a footnote that "[a]nother situation in which market forces

*At least one federal judge has attempted to minimize the requirement that a contract under this exception must be of fixed quantity. In *Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 839 F.2d 1206, 1210 (7th Cir. 1988) (Posner, J., dissenting in part), Judge Posner questioned whether the reference in *Illinois Brick* to "fixed quantity" was intended to state an independent requirement of the cost-plus exception or merely to describe a normal contract situation. *Id.* at 1211. As the majority in *Panhandle Eastern* noted, the *Illinois Brick* Court "regarded the predetermination of quantity as an essential element of the exception." *Id.* at 1209. Furthermore, as earlier discussed in this opinion, the *Hanover Shoe* Court originally imposed as an element of the pass-on defense a showing that

(Continued on following page)

have been superseded and the pass-on defense might be permitted is where the direct purchaser is owned or controlled by its customer," *id.* at 736 n.16, although the Court did not explain the parameters of the "control" necessary to fall within this exception.

The *Illinois Brick* Court expressly considered permitting several vertical levels of injured persons to bring one lawsuit against the alleged wrongdoers (*i.e.*, as in the present case with direct and indirect purchasers), a seemingly logical, efficient, and fair way to allocate the totality of damages suffered as a result of antitrust activity. The allure of this procedure did not impress the Supreme Court:

> Permitting the use of pass-on theories under § 4 essentially would transform treble-damages actions into massive efforts to apportion the recovery among all potential plaintiffs that could have absorbed part of the overcharge—from direct purchasers to middlemen to ultimate consumers. However appealing this attempt to allocate the overcharge might seem in theory, it would add whole new dimensions of complexity to treble-damages suits and seriously undermine their effectiveness.

431 U.S. at 737. The Court's subsequent discussion of the difficult economic analyses that would have to be introduced in a case involving several levels of purchasers dis-

Footnote continued—

total sales had not declined as a result of the increase in price precipitated by illegal antitrust activity. Both *Illinois Brick* and *Hanover Shoe* permit assertion of the pass-on defense only when the ultimate demand by consumers is perfectly inelastic—as in the case of existing fixed-quantity contracts—because of the "serious problems" in measuring the relative elasticities of demand. *Illinois Brick*, 431 U.S. at 742; *Hanover Shoe*, 392 U.S. at 493.

plays some fears that admittedly would not be present under the facts of this case. For instance, the Court noted the possibly incalculable effect that imperfectly competitive markets might have on the determination of damages, such as when direct purchasers compete with sellers who have not been subject to the overcharge. Of course, in the public utility area, the complete lack of competition eliminates this problem. The fact that the alleged antitrust activity took place in the context of a public utility direct purchaser renders inapplicable much of the rationale behind the decisions in *Illinois Brick* and *Hanover Shoe*, both of which involved manufactured goods in the free market. Moreover, the concern that the plaintiff's damages be proximately caused by the kind of antitrust activity that Congress contemplated in section 4, as expressed by a subsequent Supreme Court opinion, is significantly allayed in this case, where *the fact* of actual monetary injury to residential consumers of natural gas caused by the alleged price fixing is easily established. *See Associated General Contractors of Cal., Inc. v. California State Council of Carpenters*, 459 U.S. 465, 535-45 (1983) (discussing the requirement of proximate cause). Nevertheless, the Supreme Court recognized the inevitability of a case involving less complicated factual difficulties and endeavored to make the general rule as pervasive as possible:

> It is quite true that these difficulties and uncertainties will be less substantial in some contexts than in others. There have been many proposals to allow pass-on theories in some of these contexts while preserving the *Hanover Shoe* rule in others. . . .
>
> We reject these attempts to carve out exceptions to the *Hanover Shoe* rule for particular types of markets. . . .

> [T]he process of classifying various market situations according to the amount of pass-on likely to be involved and its susceptibility of proof in a judicial forum would entail the very problems that the *Hanover Shoe* rule was meant to avoid. The litigation over where the line should be drawn in a particular class of cases would inject the same "massive evidence and complicated theories" into treble-damages proceedings, albeit at a somewhat higher level of generality.

431 U.S. at 743-45.

In *Illinois Brick*, the Court certainly considered that by instituting direct purchasers as the injured parties with standing in an antitrust suit, some indirect purchasers who have suffered identifiable antitrust injury might be left uncompensated. The Court did not believe this to be sufficient enough to overcome the other factors supporting the *Hanover Shoe* rule. *Id.* at 745-47. This demonstrates the extreme lengths to which the Court was willing to go in simplifying the already complex nature of an antitrust lawsuit.

The Supreme Court has issued several subsequent opinions concerning the proper plaintiff in an antitrust action. *See Associated General Contractors of Cal., Inc. v. California State Council of Carpenters*, 459 U.S. 519 (1983); *Blue Shield of Va. v. McCready*, 457 U.S. 465 (1982). In *McCready*, the plaintiff was a beneficiary under an employer-sponsored health plan. The plan followed a practice of reimbursing the costs of psychotherapy administered by psychiatrists but not by psychologists. Plaintiff was treated by a psychologist, and the plan denied her claim for reimbursement. The Court held that

the plaintiff had standing to bring an antitrust lawsuit against the plan, but it found the policies of *Illinois Brick* inapplicable because in *McCready*, the plaintiff had suffered *direct* injury by the plan's refusal to pay her. 457 U.S. at 474-75. In *Associated General Contractors*, the Court found that a union does not have standing in an antitrust lawsuit brought against certain companies that induced landowners not to hire union contractors. In such a case, the coerced landowners or the union contractors have suffered the direct injury. 459 U.S. at 540-42. The case is consistent with *Illinois Brick* and relied substantially on its analysis. 459 U.S. at 543-45.

Having reviewed the relevant Supreme Court authority on the issue, the court will turn to the arguments of the parties and how they fit in the scheme of the cases discussed above.

III

First, plaintiffs States of Kansas and Missouri and the defendants [hereinafter referred to as "the opposing parties"] argue that the utilities' motions are inappropriate because there has not been sufficient discovery in this litigation to fully disclose all possible factual issues. These cases were filed in 1985 and it is now 1988. The court does not intend to permit this litigation to drag on indefinitely. Furthermore, the court will not withhold disposition of the motions to strike or for partial summary judgment based on a possible or speculative issue of fact which the opposition has yet to determine. If the utilities can demonstrate the existence of all necessary, uncontroverted facts, there is no legal justification in withholding judgment, whether discovery has proceeded for twenty days or twenty years.

Along this same vein, the opposing parties ask the court to defer ruling on the issue because if facts or the law subsequently develop such that dismissed parties must be brought back into the litigation, the remaining parties will be prejudiced. The court believes that if the current state of the law requires dismissal, it would be inappropriate to defer a ruling based again on a possible change in the law or in the course of the litigation.

The principal alleged unestablished factual issue is whether the utilities passed on the entirety of any allegedly illegal overcharge. The opposing parties contend that if the facts establish that the rate systems governing the utilities permitted a total pass-through of any price increase (provisions titled "energy cost adjustment" or "purchased gas adjustment"), the arrangement would constitute the functional equivalent of the "cost-plus" contract exception recognized by *Hanover Shoe*. The parties appear to be asking for a "perfect pass-on" exception to the *Hanover Shoe* "no pass-on" rule. The argument for which the opposing parties now request additional discovery is precisely the argument that the Supreme Court overruled in *Hanover Shoe*. The Court expressly considered the situation in which a direct purchaser has passed on the *entire* illegal overcharge, and it rejected any dispositive effect this fact would have. 392 U.S. at 489-91 & n.8. Other federal court decisions have recognized this and similarly held an absolute passing-on of an overcharge not to be dispositive. *Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line*, 839 F.2d 1206, 1209 (7th Cir. 1988) ("[T]here could be a 'functional equivalent' of a cost-plus contract for a fixed quantity only where factors . . . made inevitable an exact passing on of price variation *applied to a predetermined quantity* . . . .) (emphasis added); *Carter v. Berger*, 777 F.2d 1173, 1175 (7th Cir.

1985) ("[T]he direct purchaser recovers from the wrongdoer the full overcharge, trebled, even if it also recovered the whole overcharge by raising its own prices."). The court does not believe it necessary to wait upon evidence establishing the degree to which the utilities passed on the overcharge, when the Supreme Court has already disregarded its impact. In fact, under the Supreme Court's analysis, the only factual issue that would have relevance here is whether the delivery of natural gas to consumers was made pursuant to fixed quantity contracts. However, both sides agree that consumer demand for natural gas is governed neither by a fixed-quantity contract nor by anything resembling its "functional equivalent."

Besides the cost-plus contract exception, the parties opposing the present motions have attempted to assert several other exceptions. The first is the control exception noted by the Supreme Court in *Illinois Brick*: An indirect purchaser is a proper party when the direct purchaser is owned or controlled by its customer (or vice versa, as other federal courts have held). The Sixth Circuit has read this exception as being limited to relationships "involving such functional economic or other unity between the direct purchaser and . . . the defendant . . . that there effectively has been only one sale." *Jewish Hosp. Ass'n v. Stewart Mechanical Enter., Inc.*, 628 F.2d 971, 975 (6th Cir. 1980), *cert. denied*, 450 U.S. 966 (1981). The court does not believe that even a colorable claim can be made to economically tie these public utilities so closely to residential consumers that the relationship is within that contemplated by the Supreme Court. The utilities are for-profit, publicly held corporations and simply do not fit within this exception.

The second exception asserted by the opposing parties, and one that has not been addressed by the Supreme

Court, is not really an "exception" at all. The theory is that when the direct purchaser participated in the allegedly illegal activities, the indirect purchaser would be the proper plaintiff. Of course, if a direct purchaser utility has participated in antitrust activity, it should be a named defendant just as the pipeline company is in the present case. In such a situation, residential and industrial consumers would become the "direct purchasers" for purposes of the *Hanover Shoe* analysis, because they would be the first purchasers outside the conspiracy. They would not be considered "indirect purchasers" at all. Clearly, all parties in the present litigation are operating under the premise that the utilities hold the status of "direct purchasers," although the predecessors of Williams Natural Gas Company were in fact the first purchasers of natural gas from the producers. Because the pipeline company is alleged to have participated in the conspiracy, the utilities are considered the direct purchasers. The court has been shown no credible evidence that the utilities were part of the antitrust conspiracy in this case, nor has any such claim been filed in this suit. Therefore, the co-conspirator theory is inapplicable.

The opposing parties' arguments have failed to convince this court of the inapplicability of *Hanover Shoe* and *Illinois Brick*. It is not a result of irrational, dogmatic adherence to precedent that this is so. There are principled reasons why the pass-on defense should not be permitted in this case. For example, the Supreme Court recognized that a goal of the antitrust laws is compensating the victims of antitrust activity. *Illinois Brick*, 431 U.S. at 746. In fact, in his dissent from *Illinois Brick*, one of Justice Brennan's main concerns was that by denying the pass-on defense, "[i]njured consumers are precluded from recovering damages from manufacturers." *Id.* at 749

(Brennan, J., dissenting). However, any recovery by the utilities in this case will be passed on in substantial part to the consumers. The ratemaking authorities adjust the utilities' charges after considering all sources of income and expense. If the utilities prevail on their antitrust claim, their recovery will be passed on to the consumers either through a reduction in prices or through a rebate. This appears to be an eminently fair and efficient means of apportioning any damage award, much more so than through protracted litigation.

Additionally, the Supreme Court expressed concern that by including indirect purchasers, the ensuing "massive and complex damages litigation not only burdens the courts, but also undermines the effectiveness of treble-damages suits." *Associated General Contractors*, 459 U.S. at 545. Moreover, the participation of indirect purchasers "would increase the overall costs of recovery by injecting extremely complex issues into the case." *Illinois Brick*, 431 U.S. at 745. Regardless of the opposing parties' representations that disposing of the pass-on defense would not affect the complexity of the litigation, the court believes that the more focused the issues become, the less time and expense this litigation will produce, ultimately benefitting all interests. The residential consumer will receive a greater benefit if attorney's fees and costs are held to a minimum.

The court is by no means going out on a limb in confirming the applicability of *Hanover Shoe* to these facts. Just recently the Seventh Circuit came to the same conclusion on almost identical facts. In *Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 839 F.2d 1206 (7th Cir. 1988), the court agreed that in a case involving a public utility which asserted an antitrust claim against a natural gas pipeline, many of the Supreme Court's con-

cerns in *Hanover Shoe* and *Illinois Brick* were not as prevalent, such as the avoidance of multiple recoveries or the complexity of an economic determination of damages. The court held, however, that "*Illinois Brick* did not . . . leave it to the discretion of the lower courts to expand the exceptions to include situations within some range of approximation of the exceptions defined in *Illinois Brick*." *Id.* at 1210. This court agrees with the analysis and decision in *Panhandle Eastern*.

For the reasons outlined above, the court finds that partial summary judgment is proper on the pass-on defense. In so finding, the court does not intend to determine the validity of a standing defense or other defense which relies on an allegation that any damages have not been the result of the type of antitrust injury contemplated by the statute, or a defense that the defendants have not engaged in antitrust activity. The court only holds that the defendants may not use the pass-on defense in arguing that any injury produced by the alleged activity has been passed through to residential and industrial consumers.

The court also is not inclined to grant Utilicorp's other requests to strike. To the extent that any defense raised by defendants is inapplicable to Utilicorp or any other plaintiff, the court directs defendants to clear up their positions in the final pretrial order. If at that time defendants persist in asserting defenses that any of the plaintiffs find inapplicable, an additional motion for summary judgment may be filed.

IV.

The result reached by the court presents a problem as to the status of the States of Missouri and Kansas. The

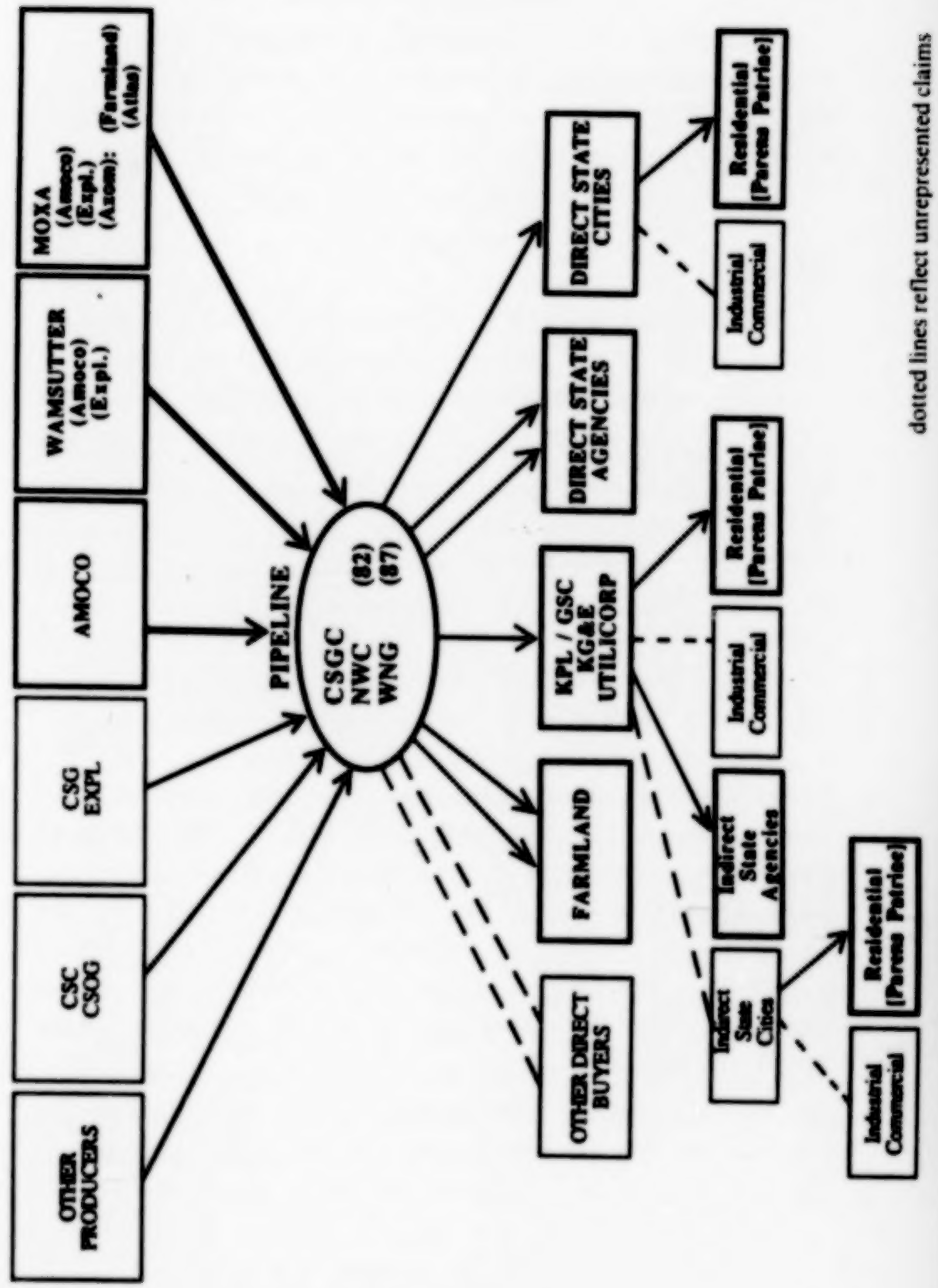
court has determined that the utilities are the proper parties to assert the antitrust claim relating to natural gas delivered to residential consumers, if indeed any compensable antitrust injury has been incurred. While it may be true that the residential consumers represented by the States have suffered actual tangible injury, "[a] showing of antitrust injury is necessary, but not always sufficient, to establish standing under § 4, because a party may not be a proper plaintiff under § 4 for other reasons." *Cargill, Inc. v. Monfort of Colo., Inc.*, 93 L. Ed. 2d 427, 436 n.5 (1986). Having determined that the treble damage remedy is not afforded to residential and industrial indirect purchasers, these persons do not have standing in this lawsuit. Dismissal of these claims need not await further briefing, because all participants in this lawsuit have recognized that the utilities' motions were, in reality, motions to dismiss the States of Kansas and Missouri in their *parens patriae* capacity. Therefore, the court will dismiss the *parens patriae* claims asserted by the States of Kansas and Missouri.

IT IS BY THE COURT THEREFORE ORDERED that plaintiffs Utilicorp, KG&E, and KP&L's motions for partial summary judgment be granted solely on the pass-on defense. IT IS FURTHER ORDERED that plaintiffs' motions to strike be denied. IT IS FURTHER ORDERED that the claims of the States of Kansas and Missouri as *parens patriae* for their citizens who purchased natural gas from a public utility be dismissed for lack of standing.

DATED: This 4th day of May, 1988, at Kansas City, Kansas.

/s/ Dale E. Saffels
Dale E. Saffels
United States District Judge

APPENDIX



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APPENDIX D

(Filed June 7, 1988)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF KANSAS

CIVIL ACTION NO. 85-2349-S &
CONSOLIDATED CASES

IN RE

WYOMING TIGHT SANDS ANTITRUST CASES

MEMORANDUM AND ORDER

On May 4, 1988, the court issued a Memorandum and Order effectively disposing of the States of Kansas and Missouri's *parens patriae* claims in the above-captioned litigation. In support of the decision, the court cited *State of Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 839 F.2d 1206 (7th Cir. 1988). The States of Kansas and Missouri now represent to the court that the opinion in *Panhandle Eastern* has been withdrawn and a motion for rehearing en banc has been granted. The States ask this court alternatively to (1) vacate and rehear or reconsider the opinion of May 4, (2) designate the order as final and appealable under Federal Rule of Civil Procedure 54(b), or (3) certify the issue to the Tenth Circuit Court of Appeals pursuant to 28 U.S.C. § 1292(b). Plaintiffs Utilicorp and KP&L would oppose reconsideration but would acquiesce in an order under 54(b) or 1292(b).

The court finds certification under 1292(b) to be appropriate in this situation. That statute states in relevant part:

> When a district judge, in making in a civil action and [sic] order not otherwise appealable under this section, shall be of the opinion that such order involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation, he shall so state in writing in such order.

The May 4 Memorandum and Order is not otherwise appealable, because it resolves less than all the claims of less than all the parties, and the court is not inclined to permit interlocutory appeal under Rule 54(b). Furthermore, as is evident from the court's order and from the recent action of the Seventh Circuit, the legitimacy of a *parens patriae* claim in this litigation is certainly an area of dispute to which the Tenth Circuit has not spoken. This issue controls several claims of Kansas and Missouri, and an immediate appeal could avoid the possibility of having to conduct two trials in this extremely complex litigation. The facts of this case present precisely the type of situation contemplated by Congress in section 1292(b).

Therefore, the court will certify the following question to the Tenth Circuit Court of Appeals:

> In a private antitrust action under 15 U.S.C. § 15 involving claims of price fixing against the producers of natural gas, is a State a proper plaintiff as *parens patriae* for its citizens who paid inflated prices for natural gas, when the lawsuit already includes as plaintiffs those public utilities who paid the inflated prices upon direct purchase from the producers and who subsequently passed on most or all of the price increase to the citizens of the State?

Pursuant to 28 U.S.C. § 1292(b), this certification shall not stay the proceedings in this court.

IT IS BY THE COURT THEREFORE ORDERED that the States of Kansas and Missouri's joint motion for certification pursuant to 28 U.S.C. § 1292(b) be granted; IT IS FURTHER ORDERED that all other requested relief be denied.

DATED: This 7th day of June, 1988, at Kansas City, Kansas.

/s/ Dale E. Saffels
Dale E. Saffels
United States District Judge

APPENDIX E

STATE OF ILLINOIS ex rel. Neil F. HARTIGAN, Attorney General of the State of Illinois, in its proprietary capacity, in its *parens patriae* capacity, and in its representative capacity, Plaintiff-Appellee,

v.

PANHANDLE EASTERN PIPE LINE COMPANY,
Defendant-Appellant.
No. 85-2601.

United States Court of Appeals,
Seventh Circuit.

Argued Feb. 28, 1986.
Decided Jan. 22, 1988.
Rehearing En Banc May 26, 1988.
Decided July 18, 1988.

State brought antitrust action on behalf of consumers of natural gas provided by distributor against interstate supplier of gas seeking damages as result of overcharges. The United States District Court for the Central District of Illinois, Michael M. Mihm, J., denied supplier's motion to dismiss, and supplier sought permission to appeal. The Court of Appeals, Fairchild, Senior Circuit Judge, 839 F.2d 1206, reversed. The full court granted rehearing en banc. On rehearing, the Court of Appeals, Posner, Circuit Judge, held that: (1) state could maintain antitrust suit on behalf of residential consumers of gas under cost-plus exception to general rule prohibiting actions by indirect purchasers, and (2) state could not maintain antitrust action for damages on behalf of industrial customers.

Affirmed in part and reversed in part.

Cudahy, Circuit Judge, concurred and filed opinion.

Fairchild, Senior Circuit Judge, concurred in part, dissented in part, and filed opinion in which Bauer, Chief Judge, and Cummings and Manion, Circuit Judges, joined.

1. Monopolies (Key) 28(1, 6)

State could maintain antitrust suit on behalf of residential consumers of gas distributor against gas supplier alleged overcharging of distributor under cost-plus exception to general rule prohibiting actions by indirect purchasers for supplier's alleged overcharging of distributor; residential customers had cost-plus pricing with direct purchaser, and that pricing was imposed by public utility regulation.

2. Monopolies (Key) 28(1.6)

State could not maintain antitrust action for damages on behalf of industrial customers of gas distributor against gas supplier for supplier's alleged overcharging of distributor, where full amount of any overcharge was not passed on to industrial customers.

Paul H. LaRue, Chadwell & Kayser, Ltd., Chicago, Ill., for defendant-appellant.

Richard L. Miller, Burke & Smith, Chtd., Chicago, Ill., for plaintiff-appellee.

Before BAUER, Chief Judge, CUMMINGS, CUDAHY, POSNER, COFFEY, FLAUM, RIPPLE, MANION, and KANNE, Circuit Judges, and FAIRCHILD, Senior Circuit Judge.*

POSNER, Circuit Judge.

*Circuit Judges WOOD, Jr. and EASTERBROOK did not participate in the consideration or decision of this case.

Central Illinois Light Company (CILCO) is a publicly regulated retail distributor of natural gas. It bought natural gas from Panhandle Eastern Pipe Line Company at prices allegedly inflated because of violations of the antitrust laws by Panhandle, and resold the gas to residential and industrial consumers. In its resales to residential consumers, CILCO passed on the entire overcharge in the form of higher rates. In 1984 the State of Illinois brought this federal antitrust suit on behalf of CILCO's customers against Panhandle—which moved to dismiss the suit as barred by the "indirect purchasers" rule of *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481, 88 S.Ct. 2224, 20 L.Ed.2d 1231 (1968), and *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 97 S.Ct. 2061, 52 L.Ed.2d 707 (1977). The district court denied the motion, but certified its order of dismissal for an immediate appeal under 28 U.S.C. § 1292(b), and we agreed to hear the appeal. A panel of this court reversed the district court and directed it to dismiss the complaint. 839 F.2d 1206 (7th Cir.1988). The full court granted rehearing en banc to decide whether regulatory cost-plus pricing can ever be excepted from the rule that "indirect purchasers" (CILCO's customers are indirect purchasers from Panhandle, CILCO being the direct purchaser) are barred from obtaining antitrust damages from their indirect seller. While the appeal was pending in this court, the district judge conducted a 13-week trial on liability, but he has deferred making a decision until we decide the appeal.

In *Hanover Shoe* the Supreme Court held that it is not a defense to an antitrust damages action that a buyer forced to pay a higher price because of the seller's antitrust violation passed on the cost of the violation to the buyer's customers (the seller's indirect purchasers) by raising his prices to them, unless the buyer had a cost-plus

contract with these customers. *Illinois Brick* announced a corollary to *Hanover Shoe*: the indirect purchaser cannot sue to recover the part of the overcharge that the buyer passed on to him. The Court again recognized an exception for the cost-plus contract, noting that it insulates the direct purchaser from "any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price." *Id.* at 736, 97 S.Ct. at 2069-70. Fastening on the words "fixed quantity," the panel majority in this case held that the cost-plus exception is never available when the indirect purchasers are free to vary the quantity they buy from the direct purchaser. The question for decision today is whether the exception is as confined as the panel thought.

The panel's opinion was not the first to read the exception so narrowly. See *Mid-West Paper Products Co. v. Continental Group, Inc.*, 596 F.2d 573, 577 n. 9, 580 (3d Cir.1979); *In re Midwest Milk Monopolization Litigation*, 730 F.2d 528, 533 (8th Cir.1984); *Lefrak v. Arabian American Oil Co.*, 487 F.Supp. 808, 819 (E.D.N.Y. 1980); cf. *Arizona v. Shamrock Foods Co.*, 729 F.2d 1208, 1212 n. 2 (9th Cir.1984); but see *In re Uranium Antitrust Litigation*, 552 F.Supp. 518 (N.D.Ill.1982). And its reading was followed in *In re Wyoming Tight Sands Antitrust Cases*, No. 85-2349-S (D.Kan. May 4, 1988). Yet it was not dictated by precedent. Not only had the prior cases all involved privately negotiated cost-plus contracts rather than cost-plus contractual provisions required by public utility regulation, but there was no reason to believe that the reference to "fixed quantity" in the Supreme Court's opinion in *Illinois Brick* was intended to govern cases so remote from the actual arrangements under scrutiny in that case. The case did not involve a fixed-quantity contract; indeed,

it did not involve a cost-plus contract, but merely an argument (which the Court rejected, see 431 U.S. at 744, 97 S.Ct. at 2074) that a buyer's practice of rule-of-thumb cost-plus pricing should be enough to allow his customers to sue the seller. Certainly there is no indication that by using the words "fixed quantity" the Supreme Court meant to address the issue of the status of regulatory cost-plus pricing. We do a disservice to the Court by wrenching its words out of context and giving them a talismanic significance; we make language a trap rather than a mode of communication. The Supreme Court has never adverted to the issue involved in the present case, and we must consider that issue in relation to the rationale of *Illinois Brick* rather than to isolated phrases in the Court's opinion. If we are to play the language game to which Panhandle invites us, moreover, then we must consider isolated phrases in other Supreme Court opinions, notably the majority opinion in *Blue Shield of Virginia v. McCready*, 457 U.S. 465, 474-75, 102 S.Ct. 2540, 2545-46, 73 L.Ed.2d 149 (1982), where the concern behind *Hanover Shoe* and *Illinois Brick* is described as "the risk of duplicative recovery engendered by allowing every person along a chain of distribution to claim damages arising from a single transaction that violated the antitrust laws." There is, as we shall see, no such risk in this case, at least so far as the residential purchasers from CILCO are concerned; and it is only they who have, in our view, a persuasive claim to be entitled to sue.

Although several district courts have rejected an exception for cost-plus rate regulation, see (besides *Tight Sands*) *Go-Tane Service Stations, Inc. v. Ashland Oil, Inc.*, 508 F.Supp. 200, 204 (N.D.Ill.1981); *City of Cleveland v. Cleveland Electric, Illuminating Co.*, 538 F.Supp. 1320, 1323-27 (N.D.Ohio 1980); *U.S. Oil Co. v. Koch Refining*

Co., 518 F.Supp. 957, 962-63 (E.D.Wis.1981), the cases are distinguishable; and in the case with facts most like those of the present case the court held that indirect purchasers could sue because public utility regulation had created "a straight cost passthrough." *In re New Mexico Natural Gas Antitrust Litigation*, 1982-1 Trade Cases ¶ 64,685, at p. 73,722 (D.N.Mex.1982) [available on WESTLAW, 1982 WL 1827]. Cf. *County of Oakland v. City of Detroit*, 628 F.Supp. 610, 613 (E.D.Mich.1986); *Illinois v. Borg, Inc.*, 548 F.Supp. 972, 975-76 (N.D.Ill.1982). An additional wrinkle in the *New Mexico Natural Gas* case, however, was that the direct purchasers were in cahoots with the defendants; this was an independent ground for allowing the indirect purchasers to sue.

It is possible to allow indirect purchasers to sue in a case such as the present one without embracing the ill-defined "functional equivalent" approach of *In re Beef Industry Antitrust Litigation*, 600 F.2d 1148 (5th Cir. 1979); see also, e.g., *Gulf Oil Corp. v. Dyke*, 734 F.2d 797, 809 (T.E.C.A. 1984). That approach—effectively criticized in *In re Midwest Milk Monopolization Litigation*, 529 F.Supp. 1326, 1337-38 (W.D.Mo.1982), aff'd, 730 F.2d 528 (8th Cir.1984); Comment, *A Legal and Economic Analysis of the Cost-Plus Contract Exception in Hanover Shoe and Illinois Brick*, 47 U.Chi.L.Rev. 743, 756-70 (1980), cf. *Abbotts Dairies Division of Fairmont Foods v. Butz*, 584 F.2d 12, 16-17 (3d Cir.1978), and found to be inapplicable to conditions in the beef industry itself in *In re Beef Industry Antitrust Litigation*, 710 F.2d 216, 219-20 (5th Cir.1983)—requires elaborate analysis of the incidence of a cost increase, which is precisely the analysis that the Court disparaged in *Illinois Brick*. Our approach does not require this. We have formal cost-plus pricing in this case rather than its "functional equivalent." We

have formal cost-plus pricing, and more: a contract that required 100 percent passing on, and an acknowledgment of 100 percent passing on in every kilowatt hour resold to CILCO's residential consumers.

To determine whether (or to what extent) this case is within the rule of *Illinois Brick*, we must consider the reasons for confining the right to sue to the direct purchaser; for it is the reasons behind a rule that determine its scope. First, because the direct purchaser is closer to the violation and hence more likely to discover it, we want to make sure that he has a strong incentive to bring the violator to book, and we do this by holding out to him the prospect of recovering the entire damages caused by the violation if he wins the suit. Second, it is difficult to apportion damages between direct and indirect purchasers by the methods of litigation. A direct purchaser who finds himself paying a higher price for inputs would love to pass on all of the additional cost to his customers in the form of a higher price, but he cannot do so, because a price that much higher will so reduce the demand for his product that his profits will fall unacceptably. (If the higher price were optimal, the firm would have raised its price without waiting for its costs to increase.) The optimal adjustment by an unregulated firm to the increased cost of the input will always be a price increase smaller than the increase in input cost, and this means that the increased cost will be divided between the two tiers, the direct and indirect purchasers—but in what proportions will often be hard to determine, even by sophisticated techniques of economic analysis. This is a central insight of the *Illinois Brick* decision. An additional complication that further demonstrates the wisdom of the decision is that the higher input price may induce the direct purchaser to use more of an alternative input, and

this substitution will affect the proportion of the initial overcharge that the direct purchaser can recoup.

Where the direct purchaser has a cost-plus contract with his customers that requires them to buy a fixed quantity, the reasons for confining the right to seek damages to the direct purchaser cease to be fully persuasive. There is no longer a problem of apportionment, because the whole of any price increase will have been passed on to the customers by virtue of the contract. Yet the second reason for confining the right to seek damages to the direct purchaser survives: he has better information about the violation. And despite the cost-plus nature of the contract, he has everything to gain from suing. He will not have to share any of the damages that he recovers with his customers unless the contract contains a clause (or a court is persuaded to adopt an imaginative conception of unjust enrichment) that entitles them to any rebate he might receive, probably years later, on an input used in performing his side of the bargain. Nevertheless the Supreme Court has said that the indirect purchaser may sue if he has a cost-plus contract with the direct purchaser.

In the present case, where cost-plus pricing is imposed by public utility regulation rather than by a purely private, purely voluntary contract, the reasons balance out slightly differently, but the case for applying the cost-plus exception of *Illinois Brick* is no weaker once the balance is restruck. The public utility has less to gain from suit than the direct purchaser in the case of the purely private contract. The public utility commission may force the utility to pass on to the consumers any and all damages that the utility recovers, and if it does utilities will have no incentive to sue because they will have nothing to

gain from suit. In the present case CILCO finally did sue—but not until 1987, by which time the present suit was far advanced and the statute of limitations with regard to the damages incurred by residential customers in the present suit either had run or was about to run; and the CILCO case has remained dormant pending our decision of the appeal. CILCO seems a most reluctant suitor, and why shouldn't it be? It has little or nothing to gain by such a suit. Indeed, one might argue that public utility regulation (to the extent effective—admittedly a potentially big if) so far identifies a public utility with its customers as to bring the case within the separate exception recognized in *Illinois Brick* for situations in which the direct and indirect purchaser are under common control. See 431 U.S. at 736 n. 16, 97 S.Ct. at 2070 n. 16.

Although the amount of gas purchased by a utility's customers is not fixed in their contract with the utility (it would be absurd for consumers to commit to a fixed quantity; their need for gas varies with the weather!), the special character of a public utility eliminates the problem of apportionment, here with respect to the only class of customers that we believe should be allowed to sue, the residential customers. The retail distribution of natural gas through a grid of pipes to the customers' homes or places of business is a natural monopoly, *Omega Satellite Products Co. v. City of Indianapolis*, 694 F.2d 119, 123, 126 (7th Cir.1982); so, in the absence of regulation, a gas utility would charge a monopoly price. Although the efficacy of public utility rate regulation has been questioned (see, e.g., Stigler & Friedland, *What Can Regulators Regulate? The Case of Electricity*, 5 J.Law & Econ. 1 (1962); Moore, *The Effectiveness of Regulation of Electric Utility Rates*, 36 So.Econ.J. 365 (1970)), the facts

of this case suggest, and the parties seem to agree, that residential natural-gas rates in Illinois are lower because of regulation than they would be in an unregulated market, implying that CILCO has unused monopoly power in that market, which it exploited by passing on the full overcharge by Panhandle. The situation in the industrial market is different. Some industrial consumers of natural gas have good alternatives, and as to them CILCO apparently had no unused monopoly power that would have enabled it to shift the whole of the cost increase to them. Instead CILCO sought and obtained regulatory permission to reduce its profit margin on sales to these customers, thereby offsetting in part the higher rates enabled by the automatic pass-through provision.

CILCO's dealings with its industrial customers show why the absence of a quantity provision in a contract can make a difference. Since the industrial customers were not obligated to take a fixed (or their required) quantity of natural gas, and since they had competitive alternatives, CILCO's profit-maximizing course of action was to swallow part of the overcharge rather than try to pass it on dollar for dollar in the form of higher rates. But its residential consumers unlike its industrial customers had no good alternatives to natural gas (of which CILCO was the sole purveyor), at least in the short term, and CILCO's profit-maximizing course of action was therefore to allow its rates to them to rise by the exact amount that its gas costs rose as a result of Panhandle's alleged overcharge. It was not only the absence of competition but the presence of regulation that made this the profit-maximizing course of action; regulation is a stand-in for the quantity requirement in an ordinary contract. Apparently rate regulation had succeeded in keeping CILCO's rates to a level where an increase in those rates was bound to in-

crease the firm's revenues because the price increase (1) would not be offset by an equal or greater proportional decline in its sales and (2) would lead to a reduction in the firm's total costs (consumers would buy less, even if only a little less, at the higher price). CILCO therefore had every incentive to raise its price by the full amount allowed by the regulatory commission—which was the full amount of the gas overcharge. And it did it.

The significance of the regulatory setting is that if regulation keeps a utility's rates below what it would like to charge, the utility will raise those rates by the full amount allowed by the regulatory commission unless such an increase would carry the utility above its optimum rate. An unregulated firm would not do that, since as we have noted an unconstrained profit maximizer will always find it in its best interest to swallow a part of any cost increase that it experiences unless its customers are committed to a fixed quantity. It is unclear from the record in this court how generous the commission's allowance was; the commission may have allowed CILCO to double its rates—yet even so, if regulation forced CILCO to charge half or less of its preferred price, CILCO would pass on the entire cost increase. No one suggests that CILCO in fact absorbed any part of the increase, so far as sales to its residential customers were concerned.

The mechanics of the pass-through provision are pertinent. The "Uniform Purchase of Gas Adjustment Clause" that Illinois by statute requires CILCO to include in its contracts not only entitled but directed CILCO, if it paid Panhandle an extra penny per million cubic feet of gas, to add exactly one penny to each customer's bill for every Mcf of gas sold to that customer. So if all of its customers had continued buying the same amount of gas CILCO would have suffered no loss on account of

the overcharge. To the extent that CILCO lost residential sales because it was charging a higher price—and no doubt it lost some sales—the loss was not passed on to CILCO's customers (at least in any sufficiently direct way to escape the rule of *Illinois Brick*) and hence is not a component of the customers' damages. But by the same token this is not a case where successive links in the chain of distribution are claiming damages in respect of the same transaction. There are, instead, two completely different sets of transactions. One consists of sales to CILCO followed by resale to its residential customers; on these sales the entire overcharge came to rest on the residential customers and they alone suffered damage and can (on the view we take of the case) recover damages. The other set of transactions consists of the sales that CILCO lost because some customers balked at the higher rates; on these sales (or rather nonsales) the only loser is CILCO, and only CILCO can sue. There is no suggestion that the residential customers are suing or could sue to recover incidental expenses incurred by reducing their purchases of natural gas—the cost of an extra sweater or a more efficient furnace or better insulation.

To illustrate the distinction between the two types of loss in this case, suppose that the price to CILCO's residential customers before the (alleged) overcharge by Panhandle was $1 per Mcf, the overcharge was 10¢ per Mcf, and by operation of the Uniform Purchase of Gas Adjustment Clause the retail price rose to $1.10 because CILCO made no offsetting reduction in another component of the price, as it did with its industrial customers. And suppose that at the new, higher price CILCO sold only 950,000 Mcf, while at the old price it had sold 1,000,000 Mcf, and that nothing plausibly accounts for the decrease in sales except the price increase, which induced consumers to use less gas. Cf. *Illinois Power Co. v. Commissioner*, 792 F.2d 683, 687-88 (7th Cir.1986). The loss to each consumer would be the number of Mcf he bought at the new price times 10¢; the loss to CILCO would be its lost profits on the sales it did not make.

Thus there can be no problem of apportionment in the suit on behalf of the residential customers. Those customers are not seeking damages for gas they did not buy, and the damages for the gas they did buy can simply be read off from their gas bills. (Well, almost: at the beginning of each year the utility estimates the amount of rate increase necessary to cover any increase in its gas bill, and there is an adjustment at the end of the year based on actual experience.) Since CILCO can sue for its lost sales (this may be a component of its belatedly filed suit against Panhandle, although that is unclear from the complaint), there can be more than one set of plaintiffs. But each set will be suing in respect of different sales—not, as in *Illinois Brick*, the same sales.

We have said that proof of the indirect purchasers' loss would be straightforward. Proof of CILCO's lost sales would also be straightforward—at least as straightforward as is possible in an antitrust case. It would be a matter of comparing the utility's sales before and after the increase in gas prices, after correcting for other factors besides the increase that might have affected those sales. Such correction is not always easy, but it is a conventional aspect of calculating damages in antitrust cases; it has to be done in every case where the plaintiff claims to have lost sales because of the defendant's unlawful conduct and the defendant argues that the loss was due partly or entirely to other factors. See, e.g., *Bigelow v. RKO Radio Pictures, Inc.*, 327 U.S. 251, 264, 66 S.Ct. 574, 579, 90 L.Ed. 652 (1946); *Fishman v. Estate of Wirtz*, 807 F.2d 520, 551

(7th Cir.1986); *id.* at 578 (partial dissent); *Olympia Equipment Leasing Co. v. Western Union Telegraph Co.*, 797 F.2d 370, 382-83 (7th Cir.1986). More important, it is a problem unrelated to the problem the Supreme Court wrestled with in *Hanover* and *Illinois Brick*. The Court was concerned with the situation where two purchasers of the same thing—the initial purchaser and the purchaser from the initial purchaser—are or could be complaining that both had been hurt, and the problem is to apportion the loss between them. Here only the residential consumers can complain about a loss from the overcharge on the gas they bought, while only CILCO can complain about a loss caused by the overcharge on gas that the residential consumers did not buy.

All this is not to say that *Illinois Brick* has no application to cases where the direct purchaser is subject to rate regulation. Although cost-plus is the spirit of rate regulation, the flesh is weak and often therefore the utility has considerable flexibility in pricing, much like an unregulated firm. Indeed, to the extent that it operates free from effective rate regulation—either because it faces competition which constrains its rates below the regulated level (apparently CILCO's situation with its industrial customers), or because the regulators are unable to prevent it from charging monopoly prices to its captive customers—the utility's situation is identical to that of an unregulated firm. But, if so, this will be revealed in the utility's decision to swallow some of the cost increase, as CILCO did with its industrial customers. In the case of its residential customers, regulation must have succeeded in forcing the utility to operate in a region of its demand curve where 100 percent passing on of any cost increase was the optimal strategy for the utility to follow, for that was the strategy it did follow.

With the rapid and unanticipated increases in fuel prices during the 1970s, utilities pressed for and obtained the right to include automatic fuel pass-through provisions in their contracts with customers, provisions that would allow the utility to pass on every dollar in higher prices that it paid for gas or other fuels to its customers without going through the time-consuming process of obtaining regulatory authorization to raise rates. Such provisions are also found in unregulated contracts, and should be treated the same there when the contract requires the buyer to take either a fixed quantity or his requirements, since a buyer cannot reduce his purchases under a requirements contract merely because he is dissatisfied with the terms of the contract as they have worked themselves out. See *Empire Gas Corp. v. American Bakeries Co.*, 840 F.2d 1333, 1340-41 (7th Cir.1988); *Wilsonville Concrete Products v. Todd Building Co.*, 281 Ore. 345, 352, 574 P.2d 1112, 1115 (1978); *Royal Paper Box Co. v. E.R. Apt Shoe Co.*, 290 Mass. 207, 195 N.E. 96 (1935); *Fort Wayne Corrugated Paper Co. v. Anchor Hocking Glass Corp.*, 130 F.2d 471, 473-74 (3d Cir.1942); White & Summers, Handbook of the Law Under the Uniform Commercial Code 126 (2d ed. 1980). (This example shows, by the way, why a rigid test of fixed quantity would be a senseless limitation on the cost-plus exception of *Hanover Shoe* and *Illinois Brick*—a buyer under a requirements contract does not have discretion as to the amount to take under the contract.) If on the other hand the buyer has complete flexibility as to how much to buy, a cost-plus provision is ineffectual; the buyer can always condition an agreement to buy a specific amount on the seller's agreeing to modify the contract by reducing the price. This is another reason for supposing that an agreement to take a fixed quantity, or, what is equivalent for these purposes, an

agreement to take one's requirements, is implicit in the cost-plus exception rather than an independent requirement for invoking it. The unexhausted monopoly power of a regulated utility takes the place of a fixed-quantity or requirements provision. The utility can force the whole of the cost increase through to its residential customers without sacrificing any profits, *and did so*.

[1, 2] But we do not think that the industrial customers should be allowed to sue for damages. By cutting its profit margin to them CILCO raised its price by less than the increase in gas cost, and while the division of that increase between the utility and its industrial customers is easy to ascertain—precisely because the utility was required to get approval for reducing its profit margin—we are unwilling to complicate the administration of *Illinois Brick* by trying to distinguish between difficult and easy apportionment cases. And the Supreme Court seemed unwilling to listen to such arguments. But for every cubic foot of gas bought by a residential customer, we *know* that the whole overcharge was passed on to the customers in accordance with the fuel pass-through provision of their contract with CILCO, and we know why (regulation plus the residential consumers' lack of alternatives).

It might seem an unimportant detail whether a buyer reacts to an overcharge by raising its price by less than the overcharge (as CILCO did with its industrial customers), thus losing fewer customers, or by raising its price by the full overcharge and thereby losing more customers than it would if it swallowed part of the overcharge. But in the second case the problem of apportioning losses on the same sales does not arise. It might also seem impermissible under *Illinois Brick* to inquire into

the question whether there really was 100 percent passing on; but the Court announced an exception for cases where there is a cost-plus contract, and there is such a contract here—the automatic fuel pass-through provision. Although it is not a contract for a fixed quantity or (what is equivalent for purposes of the exception) the buyer's requirements, the existence of public utility regulation is an adequate substitute in the circumstances.

True, we can never be absolutely certain that regulation has resulted in a 100 percent pass through; for all we know, CILCO would have sought a rate increase but for the gas overcharge, and by forbearing to do so in effect absorbed part of the overcharge. But by the same token, the seller under a fixed-quantity cost-plus contract might forbear to insist on a 100 percent pass through in order to curry favor with the buyer for the sake of future deals. No counterfactuals are certain, but the doubts here are too small to warrant our insisting that this potentially serious antitrust violation, which may have caused consumers of natural gas to pay almost $50 million in higher prices, shall go unremedied, as it may if we accept Panhandle's view of the scope of *Illinois Brick*. Whether the cost-plus exception might embrace other situations in which the direct purchaser has a cost-plus contract with the indirect purchasers but the contract does not require the indirect purchasers to buy a fixed quantity (or their requirements) is not a question that we need decide in this case.

The suit on behalf of the residential customers is within the scope of the cost-plus exception to the rule of *Illinois Brick* as we understand it, and we therefore affirm the denial by the district court of the defendant's motion to dismiss the complaint insofar as the complaint seeks

damages on behalf of CILCO's residential customers. We reverse insofar as the court allowed suit on behalf of the industrial customers for damages. We express no view of the antitrust merits or of the propriety of the requests for injunctive relief, and we award no costs in this court.

Affirmed in Part and Reversed in Part.

CUDAHY, Circuit Judge, concurring:

I concur without reservation in the majority's application of the *Illinois Brick* doctrine to the facts of this case. A bar to indirect purchaser suits would make very little sense if it were extended to the regulated natural gas distribution business where full purchased gas cost pass-through is incorporated in the retail rates The PGA clause transforms the transaction into the very epitome of a cost-plus contract. Likewise, because residential gas demand is inelastic in the short run due to the unavailability to residential customers of substitute fuels, a rough approximation of a fixed quantity term is present, whether or not required by *Illinois Brick*.

The Natural Gas Pipeline Association of America, in an amicus brief, argues that if the antitrust suit were left to the direct purchaser (CILCO), its regulator (the Illinois Commerce Commission) could and would direct CILCO to pass on the sums recovered to its customers. The customers would, therefore, be in as good a position as if the Attorney General had sued directly on their behalf. I believe this is essentially correct. CILCO has in fact now brought suit in this matter, presumably because the panel decision cast doubt on whether the Attorney General could maintain the action on behalf of consumers.

Under the practical facts of regulation CILCO would ordinarily have a greater incentive to bring this litigation

than economic theory suggests. An informal suggestion from its regulators that suit was appropriate to protect customers would ordinarily send CILCO to court. Further, regulation allows CILCO to recognize only its *prudently incurred* expenses for ratemaking purposes. Presumably, a distribution company's purchase of pipeline gas at prices inflated by antitrust violations could be challenged as an imprudent incurrence of operating expenses. An antitrust recovery would at least partially offset any imprudence in the initial purchasing decision. In any event, in its next rate case, the distribution company would be hard pressed to justify its payment of illegally inflated prices if neither it nor the Attorney General had sought to press the antitrust claim.

Nonetheless, I suspect that considerations such as the difficulty of settlement might lead CILCO to prefer an Attorney General's lawsuit to its own. Presumably, a settlement by the state Attorney General with the pipeline supplier would be accepted as fully arm's length and justifiable. Were CILCO to settle, however, the aggressiveness of its stance might be questioned by the regulators in light of its ongoing relationship with the supplier and, of course, its settlement would in all probability have to be approved by the regulatory authority. It therefore seems to me that, in the final balance, suit by CILCO is not necessarily preferable to suit by the Attorney General on behalf of the residential customers.

FAIRCHILD, Senior Circuit Judge, with whom BAUER, Chief Judge, and CUMMINGS and MANION, Circuit Judges, join, concurring in part, dissenting in part.

I concur in reversal as to the treble damage claims on behalf of industrial customers. I respectfully dissent from affirmance with respect to such claims on behalf of residential customers.

The residential customers purchase from CILCO, and are only indirect purchasers from Panhandle, who allegedly overcharged CILCO. Because the rates charged by CILCO reflect, approximately at least,[1] the actual cost of gas, it is claimed that the residential customers were "injured" so as to be entitled to treble damages under § 4 of the Clayton Act, 15 U.S.C. § 15,[2] by reason of the pass-on of the overcharge.

The Supreme Court has "held that, except in certain limited circumstances, a direct purchaser suing for treble damages under § 4 of the Clayton Act is injured within the meaning of § 4 by the full amount of the overcharge paid by it . . .". *Illinois Brick Co. v. Illinois,* 431 U.S. 720, 724, 97 S.Ct. 2061, 2064, 52 L.Ed.2d 707 (1977) (footnote omitted) (interpreting the rationale of *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481, 494, 88 S.Ct. 2224, 2232, 20 L.Ed.2d 1231 (1968)). *Hanover Shoe* had rejected an attempt by an antitrust defendant to establish that plaintiff direct buyer had not been "injured" within the meaning of § 4 because the direct buyer had passed on any overcharge. In *Illinois Brick,* plaintiff was asserting a claim on behalf of indirect purchasers that they had been "injured" by a pass-on of an overcharge. The Court reaffirmed *Hanover Shoe* and decided that its root principle (that, with limited exceptions, the full injury of the overcharge falls upon the direct purchaser) must apply to and prevent treble damage claims on behalf

1. The process of adjustment of rates charged by CILCO to rates paid is described in the panel opinion. 839 F.2d at 1208 n. 2.

2. Section 4 provides that

> [A]ny person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor . . . and shall recover threefold the damages by him sustained. . . .

of an indirect purchaser, as well as apply to and permit claims of a direct purchaser.

Both *Hanover Shoe* and *Illinois Brick* dealt with the question presented as one of statutory construction of § 4. Indeed in *Illinois Brick,* the Court said,

> In considering whether to cut back or abandon the *Hanover Shoe* rule, we must bear in mind that considerations of *stare decisis* weigh heavily in the area of statutory construction, where Congress is free to change this Court's interpretation of its legislation.

431 U.S. at 736, 97 S.Ct. at 2070.

Illinois Brick described only two exceptions to its general rule that the direct purchaser is injured by the full amount of the overcharge. One, "where the direct purchaser is owned or controlled by its customer," 431 U.S. at 736, n. 16, 97 S.Ct. at 2070, n. 16, is clearly inapplicable here. The other, which originated in *Hanover Shoe,* is where an overcharged direct buyer has a preexisting cost-plus contract for a fixed quantity. 431 U.S. at 736, 97 S.Ct. at 2069.

Judge Posner's opinion for this court suggests that the reference to "a fixed quantity" does not have controlling significance. *Ante,* pp. 893 and 894. Particular aspects of the *Hanover Shoe* and *Illinois Brick* opinions persuade me otherwise.

The *Hanover Shoe* opinion, in recognizing that "a preexisting 'cost-plus' contract" might provide an exception to its rule against a pass-on defense, did not expressly require a fixed quantity element. 392 U.S. at 494, 88 S.Ct. at 2232. That element may well have been implied, for the Court referred to the cost-plus contract as "thus mak-

ing it easy to prove that [the direct buyer] has not been damaged." *Ibid.* In *Illinois Brick,* Justice White, who wrote for the Court in both cases, expressly referred to the fixed quantity element and took pains to explain why it was important:

> But this Court in *Hanover Shoe* indicated the narrow scope it intended for any exception to its rule barring pass-on defenses by citing, as the only example of a situation where the defense might be permitted, a pre-existing cost-plus contract. In such a situation, the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price. The effect of the overcharge is essentially determined in advance, without reference to the interaction of supply and demand that complicates the determination in the general case.

431 U.S. at 735-36, 97 S.Ct. at 2069-70.

This court's opinion concedes that no doubt CILCO lost residential sales because of the higher price, and because of the overcharge if there was one. *Ante,* p. 896. It follows from *Hanover Shoe* and *Illinois Brick* that when some injury falls on the direct purchaser because of the overcharge, it all does.

After considering and rejecting proposed exceptions, the Court said "As we have noted, *supra* at 735-36, [97 S.Ct. at 2069-2070], *Hanover Shoe* itself implicitly discouraged the creation of exceptions to its rule barring pass-on defenses, and we adhere to the narrow scope of exemption indicated by our decision there." 431 U.S. at 745, 97 S.Ct. at 2074.

As I read *Illinois Brick,* the Supreme Court did not leave it to the discretion of the lower courts to create new exceptions for situations which fall within some range of approximation of the exceptions defined by the Court. And that is what this court appears to be doing with respect to the claims of the residential customers.